SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1924

No. 527

THE UNITED STATES, APPELLANT

vs.

HARRIET ROGERS FLANNERY AND J. ROGERS FLANNERY, EXECUTORS OF THE ESTATE OF JAMES J. FLANNERY, DECEASED

APPEAL FROM THE COURT OF CLAIMS.

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1 IN COURT OF CLAIMS OF THE UNITED STATES

HARRIET ROGERS FLANNERY AND J. ROGERS FLANNERY, Executors of the Estate of James J. Flannery, deceased,

vs.

THE UNITED STATES.

No. C–1080.

I. Petition. Filed October 8, 1923

The claimants respectfully represent:

I. The claimants are the executors of the estate of James J. Flannery, late of Pittsburgh, Pennsylvania, and file herewith a duly authenticated copy of the record of their appointment.

II. On March 1, 1913, the said James J. Flannery, now deceased, was the owner of 473 shares of the capital stock of the Flannery Bolt Company, acquired by him before March 1, 1913, the fair market price and value of which on March 1, 1913, was $275 a share, totaling $130,075. James J. Flannery sold said stock,
2 229 shares October 29, 1919; 99 shares October 30, 1919; and 75 shares October 31, 1919, all for $225 a share, receiving for said 473 shares the total sum of $106,425.

III. The Revenue Act of 1918, which was in effect during the year 1919, provided in part as follows:

> "Sec. 202. (a) That for the purpose of ascertaining the gain derived or loss sustained from the sale or other disposition of property, real, personal, or mixed, the basis shall be—
>
> "(1) In the case of property acquired before March 1, 1913, the fair market price or value of such property as of that date; * * *"

Article 1561 of Regulations 45 promulgated by the Commissioner of Internal Revenue and approved by the Secretary of the Treasury April 16, 1919, pursuant to the provisions of the Revenue Act of 1918 provided that:

> "For the purpose of ascertaining the gain or loss from the sale or exchange of property the basis is (a) its fair market price or value as of March 1, 1913, if acquired prior thereto, or (b), if acquired on or after that date, its cost or its approved inventory value. * * *"

This regulation in words and figures as aforesaid was in force when the return was made for James J. Flannery, deceased, for the taxable year 1919, as described in the next paragraph hereof.

IV. Said James J. Flannery died March 6, 1920. On or about April 12, 1920, a return of his income for the year 1919 was
3 filed pursuant to law by these executors, and in filing such return a loss was taken of $23,650, the difference between the fair market price and value on March 1, 1913, and the actual price received for said stock of the Flannery Bolt Company, and the same

was deducted in computing the net income of said taxpayer, all pursuant to said law and regulations.

V. By Treasury Decision 3206 promulgated July 28, 1921, by the Commissioner of Internal Revenue with the approval of the Secretary of the Treasury, Article 1561 of Regulations 45 was amended to read as follows:

> "ART. 1561. Basis for determining gain or loss from sale.—For the purpose of ascertaining the gain or loss from the sale or exchange of property the basis is the cost of such property, or if acquired on or after March 1, 1913, its cost or its approved inventory value. But in the case of property acquired before March 1, 1913, when its fair market value as of that date is in excess of its cost, the gain which is taxable is the excess of the amount realized therefor over such fair market value. Also in the case of property acquired before March 1, 1913, when its fair market value as of that date is lower than its cost, the deductible loss is the excess of such fair market value over the amount realized therefor. No gain or loss is recognized in the case of property sold or exchanged (a) at more than cost but at less than its fair market value as of March 1, 1913, or (b) at less than cost but at more than its fair market value as of March 1, 1913. * * *"

The petitioners contend that this amendment to Article 1561 is inconsistent with the Revenue Act of 1918 and is unlawful and void and that even if said regulation were lawful it is not lawfully to be applied retroactively to the return of the income of James
4 J. Flannery, deceased, for the year 1919, but the taxation of such income must be governed by the statute and lawful regulations in effect when the loss was sustained and when the return was made.

VI. On or about June 2, 1923, the Collector of Internal Revenue at Pittsburgh, Pennsylvania, made demand for the payment of additional taxes for the year 1919 totaling $12,875.24, of which additional assessment $9,046.98 was attributable to the disallowance of the said loss taken on the sale of the Flannery Bolt Company stock by the Commissioner of Internal Revenue, upon the authority of said amendment to Article 1561, Regulations 45, applied retroactively. These executors paid the amount so demanded under duress and with protest on June 11, 1923, and the same was duly paid into the United States Treasury. On or about July 13, 1923, these executors filed a claim for refund of said sum of $9,046.98, and the same was rejected by the Commissioner of Internal Revenue on or about September 19, 1923.

VII. No part of said sum of $9,046.98 so erroneously collected by the United States has been repaid to these executors. They have at all times borne true allegiance to the Government of the United States and have not in any way voluntarily aided, abetted or given encouragement to rebellion against said Government. They

are the sole and absolute owners of the claim herein presented. They have made no transfer or assignment of said claim or any part thereof and they are justly entitled to the amount claimed herein from the United States after allowing all just credits and set-offs.

5 VIII. Under Section 1324 of the Revenue Act of 1921 the claimants may be allowed interest at the rate of 6 per cent per annum on said sum of $9,046.98 from June 11, 1923, the date of payment under protest.

IX. The claimants, therefore, pray judgment in their favor against the United States in the sum of $9,046.98, with interest thereon at 6 per cent per annum from June 11, 1923.

HARRIET ROGERS FLANNERY and
J. ROGERS FLANNERY,
Executors of the Estate of
James J. Flannery,
By EDWARD B. BURLING.

COVINGTON, BURLING & RUBLEE,
Attorneys for Claimants.

(Jurat showing the foregoing was duly sworn to by Edward B. Burling, omitted in printing.)

6 *II. General traverse. Filed December 8, 1923*

No demurrer, plea, answer, counterclaim, set-off, claim of damages, demand, or defense in the premises, having been entered on the part of the defendant, a general traverse is entered as provided by Rule 34.

III. Argument and submission of case

On May 5, 1924, this case was argued and submitted on merits by Mr. Edward B. Burling, for plaintiffs, and by Mr. Roscoe R. Koch, for defendant.

7 *IV. Findings of fact, conclusion of law and opinion of the Court by Campbell, Ch. J. Entered May 19, 1924*

This case having been heard by the Court of Claims upon a stipulation of the facts made on the part of the plaintiff by their attorneys of record in this case, and on behalf of the Government by Mr. Robert H. Lovett, Assistant Attorney General, the court adopts the stipulation of facts which is set out below as its

FINDINGS OF FACTS

I

The plaintiffs, Harriet Rogers Flannery and J. Rogers Flannery, are the executors of the estate of James J. Flannery, deceased.

II

During his lifetime the said James J. Flannery was the owner of 423 shares of the capital stock of the Flannery Bolt Co. acquired by him before March 1, 1913, at a price of less than $225 a share. The fair market price and value of said stock on March 1, 1913, was $275 a share, totaling $116,325. James J. Flannery sold said stock October 29 to 31, 1919, for $225 a share, receiving for said 423 shares the total sum of $95,175.

III

Article 1561 of Regulation 45 promulgated by the Commissioner of Internal Revenue and approved by the Secretary of the Treasury April 16, 1919, pursuant to the provisions of the revenue act of 1918 (Treasury Decision 2831), provided:

"For the purpose of ascertaining the gain or loss from the sale or exchange of property the basis is (*a*) its fair market price or value as of March 1, 1913, if acquired prior thereto, or (*b*) if acquired on or after that date, its cost or its approved inventory value. * * *"

This regulation in words and figures as aforesaid was in force until July 28, 1921.

8 IV

James J. Flannery died March 6, 1920. On or about April 12, 1920, a return of his income for the year 1919 was filed by his executors. In filing such return a loss was claimed based on the difference between the fair market price and value on March 1, 1913, of said stock in the Flannery Bolt Co. and the actual price received for the same in 1919 by said James J. Flannery. The loss so claimed was deducted in said return in computing the net income of said taxpayer.

V

By Treasury Decision 3206, promulgated July 28, 1921, by the Commissioner of Internal Revenue with the approval of the Secretary of the Treasury, article 1561 of Regulations 45 was amended to read as follows:

"ARTICLE 1561. *Basis for determining gain or loss from sale.*— For the purpose of ascertaining the gain or loss from the sale or exchange of property the basis is the cost of such property, or if acquired on or after March 1, 1913, its cost or its approved inventory value. But in the case of property acquired before March 1, 1913, when its fair market value as of that date is in excess of its cost, the gain which is taxable is the excess of the amount realized therefor over such fair market value. Also in the case of property acquired before March 1, 1913, when its fair market value as of that date is lower than its cost, the deductible loss is the excess of such fair market value over the amount realized therefor. No gain or

loss is recognized in the case of property sold or exchanged (*a*) at more than cost but at less than its fair market value as of March 1, 1913, or (*b*) at less than cost but at more than its fair market value as of March 1, 1913. * * *"

VI

On or about June 2, 1923, the collector of internal revenue at Pittsburg, Pa., made demand for the payment of additional taxes on the income of James J. Flannery for the year 1919 totaling $12,875.24, of which additional assessment $7,440.67 was attributable to the disallowance by the Commissioner of Internal Revenue of the loss taken on the sale of the said 423 shares of Flannery Bolt Co. stock, upon the authority of said amendment to article 1561, Regulations 45. The plaintiff executors paid the amount so demanded under duress and with protest on June 11, 1923. On or about July 13, 1923, these executors filed a claim for refund, and the same was rejected by the Commissioner of Internal Revenue on or about September 19, 1923.

VII

No part of said sum of $7,440.67, based on the disallowance of the loss claimed on the sale of 423 shares of Flannery Bolt Co. stock has been repaid to the plaintiff executors. They have at all times borne true allegiance to the Government of the United
9 States and have not in any way voluntarily aided, abetted, or given encouragement to rebellion against said Government. They are the sole and absolute owners of the claim. They have made no transfer or assignment of said claim or any part thereof.

CONCLUSION OF LAW

Upon the foregoing findings of fact the court decides as a conclusion of law, that the plaintiffs are entitled to recover the sum of $7,440.67, with interest thereon at the rate of 6 per cent per annum from June 11, 1923.

It is therefore adjudged and ordered by the court that the plaintiffs recover of and from the United States the sum of seven thousand four hundred and forty dollars and sixty-seven cents ($4,440.67), with interest thereon at the rate of 6 per cent per annum from June 11, 1923.

OPINION

CAMPBELL, *Chief Justice*, delivered the opinion of the court:

James J. Flannery was the owner of 423 shares of the capital stock of the Flannery Bolt Co., acquired by him prior to March 1, 1913, at a price less than its fair market price and value was on March 1, 1913, and also less than he sold the same shares for in

October, 1919. The fair market price and value of these 423 shares on March 1, 1913, was $275 per share, making a total value of $116,325. He sold them in October, 1919, for $225 per share, receiving therefor a total sum of $95,175. The difference between the values at these two dates was a loss of $21,150. As between the original cost of the shares purchased prior to March 1, 1913, and the price received upon their sale after March 1, 1913, there was no loss.

James J. Flannery died March 6, 1920. Shortly thereafter the executors of his estate filed a return of his income for 1919, and upon this return claimed a loss based on the difference between the fair market price and value on March 1, 1913, of the stock already mentioned and the price received therefor upon its sale in October, 1919. This claimed loss was deducted in the return in computing the net income of the decedent. Thereafter, on or about June 2, 1923, the collector of internal revenue made demand upon the executors for additional taxes on the income of James J. Flannery for the year 1919, of which additional assessment $7,440.67 was attributable to the disallowance by the Commissioner of Internal Revenue of the loss on the sale of the 423 shares of stock in the Flannery Bolt Co. The additional taxes so demanded were paid by the executors under protest and duress, and on or about July 13, 1923, they duly filed with the commissioner a claim for refund which he disallowed. This suit seeks a recovery of the sum of $7,440.67, based on the disallowance of the claimed loss in the stock transaction.

The question for decision is whether under the revenue act of 1918 (40 Stat. 1057) the taxpayer in computing his net income for the year 1919 can make a deduction therefrom as for a loss sustained during the taxable year of the difference between the fair market price or value of certain corporate stock on March 1, 1913, and the price at which it was sold during 1919, this selling price being less than its value on March 1, 1913, but more than the price at which it was acquired, and the stock having been acquired before March 1, 1913.

Section 210 of the act imposes upon "the net income" of every individual a stated normal tax for the calendar year 1918, and for each year thereafter a lesser rate. Section 212 defines "net income" of an individual as meaning the gross income as defined in section 213, less the deductions allowed by section 214.

Section 213 declares what the term "gross income" includes and also provides that the term shall not include certain designated "items, which shall be exempt from taxation under this title."

Section 214, under the heading "Deduction allowed," provides that in computing net income there shall be allowed "as deductions" a number of items listed as "(1) business expenses, (2) interest on certain indebtedness, (3) taxes paid.

"(4) Losses sustained during the taxable year and not compensated for by insurance or otherwise if incurred in trade or business.

"(5) Losses sustained during the taxable year and not compensated for by insurance or otherwise if incurred in any transaction entered into for profit, though not connected with the trade or business."

There are a number of other authorized deductions.

The act anticipated the question as to what are "losses" that are thus authorized to be deducted because it prescribes a "basis for determining gain or loss," and provides:

"SECTION 202 (a). That for the purpose of ascertaining the gain derived or loss sustained from the sale or other disposition of property, real, personal, or mixed, the basis shall be—

"(1) In the case of property acquired before March 1, 1913, the fair market price or value of such property as of that date; and

"(2) In the case of property acquired on or after that date, the cost thereof * * *.

In interpreting these provisions it is a cardinal rule that the intention of Congress be given effect. Where the statute is expressed in plain and unambiguous terms, Congress should be intended to mean what they have plainly expressed. Chief Justice Marshall in *United States* v. *Fisher*, 2 Cranch 358, 386, said: "Where the intent is plain nothing is left to construction." In *St. Paul R. R. Co.* v. *Phelps*, 137 U. S. 528, 536, it is said that where a statute is clear and free from all ambiguity, the letter of it is not to be disregarded in favor of a mere presumption as to what is termed the policy of the Government, even though it may be the settled policy of a department. In *Insurance Co.* v. *Ritchie*, 5 Wall. 541, 545, the court say that when terms are unambiguous we may not speculate on probabilities of intention. And in the *State Tonnage Tax Cases*, 12 Wall. 204, 217, it is said: "Legislative enactments, where the language is unambiguous, can not be changed by construction, nor can the language be divested of its plain and obvious meaning." See *Crawford* v. *Brooks*, 195 U. S. 176, 189; *Franklin Sugar Co.* v. *United States*, 202 U. S. 580, 582; *White* v. *United States*, 191 U. S. 545, 551.

It is a primary and general rule of statutory construction that the intent of the lawmaker is to be found in the language
11 that he has used. *See Goldenberg Case*, 168 U. S. 95, 102.

In *Bates Refrigerating Co.* v. *Sulzberger*, 157 U. S. 1, 33, the following language is adopted: "It is not only the safer course to adhere to the words of a statute construed in their ordinary import, instead of entering into any inquiry as to the supposed intention of Congress, but it is the imperative duty of the court to do so." See *Lake County* v. *Rollins*, 130 U. S. 662, 670. Another familiar rule is that the statute must be construed as a whole. Its clauses are not to be segregated, but every part is to be construed with reference to every other part. See *Blair* v. *Chicago*, 201 U. S. 400, 463; *Market Co.* v. *Hoffman*, 101 U. S. 112, 115; *Pollard* v. *Bailey*, 20 Wall. 520, 525. These rules are the more applicable when it becomes the duty of a court to construe a taxing statute because such

a statute directly concerns the individual citizen as well as others, and the popular or received import of its words should furnish the general rule of its interpretation to the end that its provisions may be the better understood by those who must pay the taxes which it imposes. See *Maillard* v. *Lawrence*, 16 How. 251, 261.

In the revenue act of 1918 Congress was imposing a tax on the net income of the individual, among others, and defined gross income. It provided that in computing this taxable net income there should be allowed certain "deductions." These deductions included losses sustained during the taxable year if incurred in trade or business, of if incurred in any transaction entered into for profit though not connected with trade or business. If the question of the meaning of these deductible losses were left to section 214 alone its solution would be more difficult, but it was not permitted to rest in such uncertainty. By section 202 (*a*) a basis is established for the purpose of ascertaining the loss sustained from the sale of property, and in the case of property acquired before March 1, 1913, this basis is the fair market price or value of such property as of that date. With this value found and the sale price fixed, the loss sustained, if any, is the difference between these amounts. The subject matter of section 214 is the ascertainment of net income less certain authorized deductions. Many of these deductions are allowable only because Congress authorized them, and what deductions should be allowed is plainly a matter of legislative discretion.

The present case has to do with losses sustained, and the loss which Congress authorized to be deducted was a loss measured by the difference between the price stated at one time and another time. Manifestly the meaning of losses sustained as the words appear in section 214 is not to be determined independently of other parts of the act. Even a technical word is not construed technically where otherwise defined in the statute itself. See *Pirie* v. *Chicago Title Co.*, 182 U. S. 438, 443. Congress could have omitted the basis for determining loss, but it did not do that, and inserted section 202 instead. The losses sustained which are authorized to be deducted are losses ascertained as the act requires. It thus defines what are deductible losses. They are not required to be such as could arise if the property were sold for less than it cost. Congress could have required that such a loss be shown, but it did otherwise. It carefully distinguished between "property acquired before March 1, 1913," and property acquired on or after
12 that date. As to the former, the price or value as of March 1, 1913, governs, and as to the latter, "the cost thereof" governs. The first of these distinctions is wiped out if the cost prior to March 1 be required, and the second clause is useless if the original cost of the property must in every case be used in ascertaining the deductible loss.

A fact not to be lost sight of is that Congress has authorized deductions in computing the net income and that the statutory rule for ascertaining the loss sustained is a prescribed method of finding

these authorized deductions. This statutory rule as applicable to property acquired before March 1 does not purport to show what is called in defendant's brief an "actual" loss, by which is meant a loss based on the original cost and selling price; but as applied to property acquired on or after March 1, 1913, the statute does contemplate an actual loss before it is properly deductible. Differently expressed, the statute adopts a more or less arbitrary basis for ascertaining a "loss sustained" on property acquired before March 1, 1913, and sold after the passage of the act of 1918, and it was competent for Congress to adopt this basis and authorize the resultant deduction. Speaking for the court, Mr. Justice Harlan, in *Bate Refrigerating Co.* v. *Sulzberger*, 157 U. S. 1, 36, said: "In our judgment the language used is so plain and unambiguous that a refusal to recognize its natural, obvious meaning would be justly regarded as indicating a purpose to change the law by judicial action, based upon some supposed policy of Congress." We think it the duty of this court to give effect to the language of the enactment.

Upon the question under consideration we find no material difference between the revenue act of 1918 and the two prior enactments of 1916 and 1917, 39 Stat. 756; 39 Stat. 1000, and the view we have taken is in keeping with the regulations of the Treasury (Treas. Dec. 2831) in force until July 28, 1921. (See Treasury Decision 3206.) It is urged, however, that the cases of *Goodrich* v. *Edwards*, 255 U. S. 527, and *Walsh* v. *Brewster*, 255 U. S. 536, are decisive of the question. These cases deal with the question of "gain" in the act of 1916. They do not discuss or decide whether a loss claimed and ascertained as in this case is a proper deduction in computing net income of the individual under the revenue act of 1918. That the right to tax income and the right to authorize deductions are governed by different considerations is manifest. Our conclusion is that the plaintiffs are entitled to recover. And it is so ordered.

HAY, *Judge;* DOWNEY, *Judge*, and BOOTH, *Judge*, concur.

13 *V. Judgment*

At a Court of Claims held in the city of Washington on the nineteenth day of May, A. D. 1924, judgment was ordered to be entered as follows:

The court, upon due consideration of the premises, find in favor of the plaintiffs, and do order and adjudge that the plaintiffs, as aforesaid, are entitled to recover and shall have and recover of and from the United States the sum of seven thousand four hundred and forty dollars and sixty-seven cents ($7,440.67), with interest thereon at the rate of 6 per cent per annum from June 11, 1923.

By the Court.

VI. Petition for and order allowing appeal filed June 27, 1924

From the judgment rendered in the above-entitled cause on the 19th day of May, 1924, in favor of claimants, the defendants, by

their Attorney General, on the 27th day of June, 1924, make application for, and give notice of, an appeal to the Supreme Court of the United States.

ROBERT H. LOVETT,
Assistant Attorney General.

Ordered:

That the above application for appeal be allowed as prayed for.
June 30, 1924.

By the Court.

14 In Court of Claims

(Title omitted.)

Clerk's certificate

I, F. C. Kleinschmidt, assistant clerk Court of Claims, certify that the foregoing are true transcripts of the pleadings in the above-entitled cause; of the argument and submission of case; of the findings of fact, conclusion of law and opinion of the court by Campbell, Ch. J.; of the judgment of the court; of the defendant's application for an appeal and of the order of the court allowing said application.

In testimony whereof I have hereunto set my hand and affixed the seal of said court at Washington City this seventh day of July, A. D. 1924.

[SEAL.]

F. C. KLEINSCHMIDT,
Assistant Clerk Court of Claims.

(Indorsement on cover:) File No. 30,492. Court of Claims. Term No. 527. The United States, appellant, vs. Harriet Rogers Flannery and J. Rogers Flannery, executors of the estate of James J. Flannery, deceased. Filed July 9th, 1924. File No. 30,492.

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In the Supreme Court of the United States

OCTOBER TERM, 1924

THE UNITED STATES, APPELLANT
v.
HARRIET ROGERS FLANNERY AND J. Rogers Flannery, executors of the estate of James J. Flannery, deceased } No. 527

APPEAL FROM THE COURT OF CLAIMS

BRIEF FOR THE UNITED STATES

STATEMENT

This action was brought in the Court of Claims by the executors of the estate of James J. Flannery, deceased.

Flannery had bought 423 shares of stock of the Flannery Bolt Company before March 1, 1913, for *less* than $225.00 a share. Its value on March 1, 1913, was $275.00 a share. He sold it in October, 1919, for $225.00 a share. He died on March 6, 1920.

His executors filed a return of his income for 1919. In it they claimed a loss based on the difference between the value of the stock on March 1, 1913, and the actual price received for it in

1919. Although the stock was sold for more than it had cost, this difference of $50.00 a share was deducted in the return as a loss in computing the net income of the taxpayer.

The Commissioner of Internal Revenue disallowed the loss taken on the sale of the stock. The collector of internal revenue at Pittsburgh, Pennsylvania, demanded payment of additional taxes on the deceased's income for 1919, of which $7,440.67 was attributable to the deduction which had been made as a loss on that sale of stock. The executors paid the amount so demanded under protest on June 11, 1923. Thereafter a claim for refund was duly filed and rejected.

The executors then brought this suit in the Court of Claims to recover the said sum. That court rendered judgment in their favor. The case is here on appeal from the final judgment of the Court of Claims.

THE QUESTION INVOLVED

The question involved is whether Flannery sustained a loss in the year 1919 by selling the stock for more than it cost him, though he sold it for less than its value on March 1, 1913.

THE STATUTE

The pertinent provisions of the Revenue Act of 1918 (Act of Congress, approved February 24, 1919, 40 Stat. 1060–1067) are as follows:

> Sec. 212. (a) That in the case of an individual the term "net income" means

the gross income as defined in section 213, less the deductions allowed by section 214.

* * * * *

Sec. 214. (a) That in computing net income there shall be allowed as deductions:
* * *

(5) Losses sustained during the taxable year and not compensated for by insurance or otherwise, if incurred in any transaction entered into for profit, though not connected with the trade or business; * * *.

Sec. 202. (a) That for the purpose of ascertaining the gain derived or loss sustained from the sale or other disposition of property, real, personal, or mixed, the basis shall be—

(1) In the case of property acquired before March 1, 1913, the fair market price or value of such property as of that date; and

(2) In the case of property acquired on or after that date, the cost thereof;
* * *.

ARGUMENT

Where a taxpayer sells property for more than it cost him he is not entitled to claim a loss even though he receives less than he would have been paid for it on March 1, 1913.

It will be noted that the taxpayer derived a profit from the transaction and that the question is whether he is entitled to claim a loss because the stock sold for less in 1919 than it would have brought in 1913, where that sale was for more than the original purchase price.

In other words, can a taxpayer lessen his contribution to the Treasury by deducting a paper loss which was no loss in fact but in the instant case an actual gain? Is it conceivable that Congress, when it permitted the taxpayer to lessen his burden to the extent of an actual loss intended to enable him to profit when there was no loss in fact? Certainly the instant case presents a novel way of escaping taxation if actual profits may be charged as paper losses.

Were this a case of first impression the common sense of the proposition and the great end of taxation would seem determinative, but the question has already been decided by this Court in *Goodrich* v. *Brewster,* 255 U. S. 527, and *Walsh* v. *Brewster,* 255 U. S. 536. While the instant case presents the question from a different angle, it virtually attempts to reargue the principle involved in those two decisions.

The statute makes no distinction between gains and losses. They are grouped together and made parts of one system, for Section 202 makes the same rule applicable whether it be a "gain derived or loss sustained." Unless, therefore, this court desires to depart from its ruling in the cases just cited, it must be presumed that whether the taxpayer is credited with a loss or debited with a gain, the loss or gain must be a reality and not a fiction of bookkeeping.

In *Goodrich* v. *Edwards,* 255 U. S. 527, 535, stock worth $291,600 when acquired in 1912 and

worth $148,635.50 on March 1, 1913, was sold for $269,346.25 in 1916. The court held that no gain was realized on this investment although it had been sold for much more than could have been realized on March 1, 1913.

In *Walsh* v. *Brewster,* 255 U. S. 536, this court passed upon two transactions which are pertinent. Bonds were purchased in 1899 for $191,000 and sold in 1916 for the same amount. On March 1, 1913, their market value was $151,845. The court disregarded the value in 1913. It simply compared the original cost with the amount obtained at their sale and said that as there had been no profit on the entire period there could be no tax. Other bonds bought in 1902 and 1903 for $231,300 were worth $164,480 on March 1, 1913, and were sold in 1916 for $276,150. This court decided that the taxable gain was only the advance over the original cost and not the advance over the value on March 1, 1913.

In these cases the court held that the gains did not consist in the increase in value over that on March 1, 1913, but only the increase, if any, over the original purchase price.

The decision of the Supreme Court of New York in *Bush* v. *Law et al., State Tax Commission,* 206 N. Y. App. Div. 800, 201 N. Y. Supp. 513, is directly in point. The provisions of the New York income tax law concerning the ascertainment of gain and loss are in the same terms as those of the federal income tax law herein involved, save only

that in the New York law the date of January 1, 1919, corresponds to the date of March 1, 1913, in the federal law. In the *Bush case* property bought by a taxpayer before 1919 had increased in value until January 1, 1919, but was sold in 1919 for a much smaller sum than could have been obtained on the first of January, but still at a profit over the cost. The state tax commission assessed an income tax on the profit derived and refused to allow a deduction for the alleged loss by the sale at less than the value of January 1, 1919. On appeal this determination was confirmed by the supreme court. That court relied upon its earlier decision in *People ex rel. Klauber* v. *Wendell,* 196 N. Y. App. Div. 827, and other cases, as to gain, in which it had construed the state statute in the same manner as this court had construed the federal statute in *Goodrich* v. *Edwards* and *Walsh* v. *Brewster,* and had cited those cases, although the New York court had reached the same conclusion upon independent reasoning.

In the *Goodrich* and *Walsh* cases the court considered only actual gains between purchase and sale and not paper gains over prices which could have been obtained in March, 1913. In the New York case the supreme court of that state refused to consider paper losses, saying that only actual losses could be taken into the account.

It is submitted that there is nothing in the income tax law which justifies the conclusion that Congress intended to declare that there had been

a loss because between the time of purchase and sale there had been an intermediate higher value in 1913, in view of the decision of this court that the existence of a gain did not follow from a lower value in 1913 than the value at the time of the earlier purchase or the later sale. The Revenue Acts levying income taxes have taxed as income gains received by the taxpayer, but have allowed few deductions, so that while the words defining income or profits or gains have been general, the definitions of losses have been particular and exact. Thus under the Act of 1913 all gains were taxed as income, but only losses " incurred in trade " could be deducted. While the taxpayer must pay taxes on gains or profits from any transactions, many losses could not be deducted, as, for instance, losses from illegal transactions or losses sustained from the sale of his automobile or his residence. So that all gains have been taxed as income, but not every loss may be deducted. And in no case does it allow any deduction which is not an *actual* loss.

To return to the sections now under consideration, it seems clear that actual gains and actual losses and not paper gains or paper losses were within the purview of the act. The words " gain " and " loss " are used together throughout the act as correlative terms; the method of determining whether there has been a gain applies equally to the determination of whether there has been a loss.

In accordance with the decision in the *Goodrich* and *Walsh cases* two questions may arise:

(1) Has there been a gain or loss?

(2) If there has been a gain or loss, the extent of the gain or loss.

But in accordance with those cases the first question must be answered first. If there has been no actual gain upon the entire transaction, no income tax may be laid. If there has been no actual loss upon the entire transaction, no deduction for loss may be claimed. This court has so decided as to gain. The same rule should apply to loss.

As there was no actual loss in the present case—no more than a paper loss as compared with March 1, 1913—no further question arises. Only if an actual gain or an actual loss were proved would the computation of the amount of the gain or loss be material. Only in such a case would the 1913 value call for consideration. The wording of the statute " losses sustained " requires in unmistakable language the existence of a *loss* before anything may be deducted. Where the taxpayer has not sustained an actual loss but has made a profit on the transaction, there is no loss which he may deduct. That is the case at bar.

It was argued in the court below and that court was evidently misled by the argument, that Section 202 of the law applied to this case and showed that there was a loss. It reads:

> Sec. 202 (a). That for the purpose of ascertaining the gain derived or loss sus-

> tained from the sale or other disposition of property, real, personal, or mixed, the basis shall be—
>
> (1) In the case of property acquired before March 1, 1913, the fair market price or value of such property as of that date,

But it does not read " for the purpose of ascertaining *if there was* a gain derived or loss sustained." The question of a gain or a loss is a preliminary matter to be determined. The words " for the purpose of ascertaining *the* gain derived or loss sustained " assume that it has already been determined if a gain or a loss has occurred in the instant case.

The meaning of the statute is to be sought in the language of the act itself, the lawmaker is presumed to know the meaning of words and the rules of grammar, and no ambiguity or hidden meaning or intent is to be presumed or sought out.

In *United States* v. *Goldenberg*, 168 U. S. 95, 102, this Court said:

> The primary and general rule of statutory construction is that the intent of the lawmaker is to be found in the language that he has used. He is presumed to know the meaning of words and the rules of grammar. The courts have no function of legislation, and simply seek to ascertain the will of the legislator. It is true there are cases in which the letter of the statute is not deemed controlling, but the cases

> are few and exceptional, and only arise when there are cogent reasons for believing that the letter does not fully and accurately disclose the intent. No mere omission, no mere failure to provide for contingencies, which it may seem wise to have specifically provided for, justify any judicial addition to the language of the statute.

And in *United States* v. *Standard Brewery*, 251 U. S. 210, 217, it was said:

> Nothing is better settled than that in the construction of a law its meaning must first be sought in the language employed. If that be plain, it is the duty of the courts to enforce the law as written, provided it be within the constitutional authority of the legislative body which passed it. *Lake County* v. *Rollins*, 130 U. S. 662, 670, 671; *Bate Refrigerating Co.* v. *Sulzberger*, 157 U. S. 1, 33; *United States* v. *Bank*, 234 U. S. 245, 258; *Caminetti* v. *United States*, 242 U. S. 470, 485.

Now, it is not possible to construe the phrase "for the purpose of ascertaining the gain derived or loss sustained" to mean "for the purpose of ascertaining *if* a gain was derived or loss sustained." The phrase, in the correct use of English, which is conclusively presumed, can be applied only *after* it has been ascertained that there was a gain derived or a loss sustained. This section is of no possible aid or benefit to the tax-

payer to show that when he sold the property at a profit he thereby sustained a loss.

So it was said by this Court in construing this section with reference to gains under the Revenue Act of 1916:

> Section 2 (c) is applicable only where a gain over the original capital investment has been realized after March 1, 1913, from a sale or other disposition of property.
> *Goodrich* v. *Edwards,* 255 U. S. 527, 535.
> *Walsh* v. *Brewster, supra.*

And the same conclusion is irresistible as to a loss. In the 1918 Act the wording of this part of the phrase is exactly the same as in the 1916 Act quoted by this Court, except the words "or loss sustained" are inserted after the words "the gain derived."

It is very evident that Congress intended to establish a uniform, harmonious, and consistent basis for ascertaining gains derived and losses sustained in computing net income for purposes of taxation in the Revenue Act.

This is made even more evident in the Act of 1918 than in the Act of 1916. For in the 1916 Act, Sec. 2 (c) contains the provision "for ascertaining the gain derived," etc., and Sec. 5 (a) Fourth, contains the provision "for ascertaining the loss sustained," etc. While in the 1918 Act these are contained in one section and in one sentence, viz: "Sec. 202 (a). That for the pur-

pose of ascertaining the gain derived or loss sustained," etc. The placing of these in one sentence and in the alternative shows positively that the same transaction can not be both a gain and a loss, as is contended by the appellees, and shows that Congress intended the same general rules of construction and interpretation to apply to "gain" and "loss."

In *Goodrich* v. *Edwards* and *Walsh* v. *Brewster, supra,* this court held that the language of the Act as applied to gains means only those *actual* gains which constitute the difference between cost and selling price. It necessarily follows that there should be a similar construction of this language with respect to deductible losses. That is to say, it was intended to prevent the deduction of anything but actual losses, viz, the difference to the taxpayer between selling price and cost of the property sold. Any other holding would make practically the same language mean one thing with respect to gains derived and another thing with respect to losses sustained, thereby nullifying the plain intent of Congress.

The decisions of this Court in *Goodrich* v. *Edwards* and *Walsh* v. *Brewster, supra,* are decisive of the case at bar. Those decisions are based upon the clear, plain meaning of the Act of Congress, and necessarily follow the correct use of the English language in that Act.

CONCLUSION

It is therefore submitted that as the taxpayer derived a profit from his transaction, he cannot claim he has sustained a loss, and he is not entitled to deduct any sum for an alleged loss; that the judgment of the Court of Claims should be reversed, and that the entry of a judgment for the United States should be directed.

Respectfully submitted.

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DECEMBER, 1924.

○

JAN 3 1925
WM. R. STAGGERY

IN THE

Supreme Court of the United States

OCTOBER TERM, 1924.

No. 527.

UNITED STATES, *Appellant*,

v.

HARRIET ROGERS FLANNERY

and

J. ROGERS FLANNERY,

Executors of Estate of

JAMES J. FLANNERY, Deceased, *Appellees.*

APPEAL FROM THE COURT OF CLAIMS.

BRIEF OF APPELLEES.

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APPEAL FROM THE COURT OF CLAIMS.

BRIEF OF APPELLEES.

Statement of the Case.

James J. Flannery purchased certain shares of stock prior to March 1, 1913, which on March 1, 1913, were worth $275 per share. He sold them in 1919 for $225

per share, thus producing a loss of $50 a share when measured by the March 1, 1913, value. There was, however, no loss when measured by original cost prior to March 1, 1913. He deducted in his income tax return for 1919 the loss measured by the March 1, 1913, value, which was then permitted by the regulations of the Bureau of Internal Revenue. Subsequently the Bureau changed its regulations so that no loss was recognized beyond the extent of the loss based on cost, and an additional tax was assessed against the estate of Flannery, who had died in the meantime. His executors paid the additional tax under protest, filed a claim for refund which was disallowed and brought this suit in the Court of Claims. A judgment was rendered in favor of the executors, from which the Government has appealed to this Court. The case presents the single question whether under the Revenue Act of 1918 a taxpayer in computing his net income can use the March 1, 1913, value as the basis of determining a loss in the case of property acquired prior to that date.

Argument.

The Revenue Act of 1918 Plainly Makes the March 1, 1913, Value the Basis for Calculating Losses Regardless of Original Cost.

The Revenue Act of 1918 was in force during the year 1919 and applied to the deductions which are the subject of this suit. Section 214 permits the taxpayer to deduct from gross income among other things:

"(5) LOSSES SUSTAINED DURING THE TAXABLE YEAR AND NOT COMPENSATED FOR BY INSURANCE OR OTHERWISE, IF INCURRED IN ANY TRANSACTION ENTERED INTO FOR PROFIT, THOUGH NOT CONNECTED WITH THE TRADE OR BUSINESS * * *"

Section 202 (a) defines the losses deductible under Section 214 and is plain and unambiguous:

"THAT FOR THE PURPOSE OF ASCERTAINING THE GAIN DERIVED OR LOSS SUSTAINED FROM THE SALE OR OTHER DISPOSITION OF PROPERTY, REAL, PERSONAL, OR MIXED, THE BASIS SHALL BE—

"(1) IN THE CASE OF PROPERTY ACQUIRED BEFORE MARCH 1, 1913, THE FAIR MARKET PRICE OR VALUE OF SUCH PROPERTY AS OF THAT DATE; AND

"(2) IN THE CASE OF PROPERTY ACQUIRED ON OR AFTER THAT DATE, THE COST THEREOF; OR THE INVENTORY VALUE, IF THE INVENTORY IS MADE IN ACCORDANCE WITH SECTION 203."

The position of the taxpayer is that the language of the Act just quoted is clear and does not need interpretation. Section 202 (a) defines the losses from the sale of property which are deductible under Section 214. Where property acquired before March 1, 1913, is sold Section 202 (a) provides that the *basis* for ascertaining the loss deductible under Section 214 shall be the fair market value of the property on March 1, 1913. The definition of the word "basis" contained in Webster's dictionary is: "1. The foundation of anything. * * * 5. The first or fundamental principle."

Thus in making the value of the property on March 1, 1913, the *basis* for ascertaining the loss, Congress can only have meant that that value was the foundation upon which the determination rested, the first and

fundamental principle. If, as the Government contends, the March 1, 1913, value simply limits the amount of the loss which must first be ascertained by comparison of the selling price with original cost, then the March 1, 1913, value is not the foundation of the loss, or the first and fundamental principle of the determination--in other words, it is not the *basis*. Such a conclusion is directly contrary to the plain and specific declaration of Congress.

The declaration of Congress contained in Section 202 (a) is clear that, while the original cost is to be the basis or foundation of the loss, in the case of sales of property acquired *after* March 1, 1913, it is not to be the basis or foundation of the loss from the sales of property acquired *before* March 1, 1913, but that in such cases the basis is to be the March 1, 1913, value. In Section 202 (a) Congress established three different bases for ascertaining losses sustained from the sales of three different classes of property.

> (a) As to *all* property acquired prior to March 1, 1913, the basis for ascertaining the loss shall be March 1, 1913, value;
>
> (b) As to uninventoried property acquired after March 1, 1913, the basis shall be cost.
>
> (c) As to inventoried property acquired after March 1, 1913, the basis shall be the inventory value;

The Solicitor General says Congress meant cost to be the basis as to both classes (a) and (b) In that case why did Congress divide the section into Clauses (1) and (2)? Why did not Congress provide simply in one clause that cost should be the basis in *all* cases, if, as the Government now contends, that was its intention?

Surely, no one can read these clauses and conclude from the language used that Congress intended them to mean what the Solicitor General now contends they mean. If they must be given the meaning contended for by the Government the reason must be found outside the language employed.

The Government's argument is based on general reasoning as to the nature of losses. As a conclusive argument it asserts that what it calls "paper losses" cannot be deducted. It is not clear what is meant by the term "paper losses" and certainly the loss claimed by the taxpayer in this case was a real loss. Neither is it true that "paper losses" could not be deducted if Congress permitted it. Congress can permit any deductions it pleases. If Congress in so many words provided for the deduction of paper losses, then they could be deducted. There is only one question in the case and that is, did Congress intend that losses of the character here in question should be deducted. That question must be determined by a study of the Act of Congress and not by general reasoning or by describing the losses as "paper losses."

The Revenue Act of 1924 throws an entertaining light on the confident assertion by the Solicitor General of the existence of a general principle condemning the deduction of "paper losses." By that Act Congress deliberately decided to allow the deduction of the kind of losses which the Solicitor General's brief calls "paper losses." This decision by Congress was made in the face of the controversy over the deductibility of such losses under the 1918 Act, and constituted a reversal of the position taken by Congress in the 1921 Act in which, as is pointed out below, Congress changed the law and refused to allow the deduction of such

losses. The 1924 Act not only permits the taxpayer to deduct just such a loss as Flannery deducted, but is even more liberal than the 1918 Act. The provision in the 1924 Act is as follows:

> "204 (11) (b) The basis for determining the gain or loss from the sale or other disposition of property acquired before March 1, 1913, shall be (A) the cost of such property * * * or (B) the fair market value of such property as of March 1, 1913, whichever is greater." * * *

In the endeavor to give some explanation of Clause (1) of the 1918 Act the Solicitor General's brief suggests that it applies only after it has first been determined there has been a loss, looking at the transaction as a whole. Where the transaction as a whole did not produce a loss, so the reasoning runs, the clause does not apply. The argument is that first having ascertained there is a loss, then the deductible portion of *the* loss is ascertained by the application of Clause (1). This suggestion is not borne out by anything in the act and would produce some queer consequences as shown by the two illustrations following:

Case One. In 1905 X buys property for $100. Its March 1, 1913, value is $1,000. In 1919 he sells it for $100.

Case Two. In 1905 X buys property for $100. Its March 1, 1913, value is $1,000. In 1919 he sells it for $99.

In the first case, according to the Solicitor General's brief, there is no loss on the whole transaction and although there is a loss using the March 1, 1913, value as a basis, Clause (1) does not apply and no deduction is allowable.

The second case, of course, is just like the first except for the insignificant variation that the sale in 1919 is for $99 instead of $100, thereby producing a loss of $1 taking the transaction as a whole. And yet, according to the Solicitor General's theory, that would be enough to cause Clause (1) to apply, permitting a deduction of the difference between the March 1, 1913, value and the selling price of $99, in the case supposed a loss of $901.

To avoid this absurd conclusion the Solicitor General will have to claim that Clause (1) is to be construed as though it limited the deductible loss to cases where there is a loss on the whole transaction and had a further limitation that even then the March 1, 1913, value shall not apply where that is more than cost. But there is nothing in the act justifying that. Plainly Congress meant that March 1, 1913, value should be the basis in *some* cases. We say it is to be the basis in *all* cases where property was purchased prior to that date. The Solicitor General, if he rejects our contention, must say in what cases it is to be the basis. We understand him to say that the March 1, 1913, value is the *basis* whenever in the case of property purchased prior to that date there is a loss on the whole transaction. And if he does say that, then we reach the absurd consequences developed by the two illustrations above.

A Comparison with the Language of the Revenue Act of 1921 Confirms the Construction Placed by the Taxpayer on the Revenue Act of 1918.

Had it been intended in the Revenue Act of 1918 that the original cost of property acquired prior to

March 1, 1913, was to be material in determining a loss, it would have been very easy to say so. For purposes of comparison Section 202 of the Revenue Act of 1921 may be cited, which provides:

> "(a) That the basis for ascertaining the gain derived or loss sustained from a sale or other disposition of property, real, personal, or mixed, acquired after February 28, 1913, shall be the cost of such property; * * *
>
> "(b) The basis for ascertaining the gain derived or loss sustained from the sale or other disposition of property, real, personal, or mixed, acquired before March 1, 1913, shall be the same as that provided by subdivision (a); but—
>
> "(1) If its fair market price or value as of March 1, 1913, is in excess of such basis, the gain to be included in the gross income shall be the excess of the amount realized therefor over such fair market price or value;
>
> "(2) If its fair market price or value as of March 1, 1913, is lower than such basis, the deductible loss is the excess of the fair market price or value as of March 1, 1913, over the amount realized therefor; * * *"

It will be noted that the Revenue Act of 1921 (which was *not* in force in or for the year 1919) provided primarily that the basis for ascertaining gain or loss should be *the same* whether the property was acquired prior to or after March 1, 1913, and that such basis should be cost. Only if a gain or loss was established as compared with the original cost did the value on March 1, 1913, have any application, and then such value might reduce but could not increase such gain or loss for purposes of taxation.

The Revenue Act of 1918, on the contrary, provided

just as clearly for *different* methods of determining loss in the case of property acquired before and in the case of property acquired after March 1, 1913. As to property acquired prior to March 1, 1913, the basis in all cases was to be value on March 1, 1913. As to property acquired after March 1, 1913 (except inventoried property), the basis was to be cost.

Under the construction contended for by the Government there would be no difference in the meaning of the loss provisions of the Revenue Acts of 1918 and 1921. If so, why was the language changed? As was said by the Court in United States v. Hammers, 221 U. S. 220, 226:

> "* * * a change in the provisions of an act usually indicates, or is intended to indicate, a change of purpose, to enlarge or restrict the provisions of the prior law."

The Allowance of a Loss Under the Revenue Act of 1918, Based on March 1, 1913, Value Is Consistent With the Continued Practice of the Bureau of Internal Revenue under the Prior Revenue Acts.

The Revenue Act of 1909, effective January 1, 1909, had placed a tax on all corporations measured by their incomes. Although practically an income tax on corporations prior to the Sixteenth Amendment, it had been sustained as an excise tax based on income. Flint v. Stone-Tracy Co., 220 U. S. 107.

The Sixteenth Amendment to the Federal Constitution under which the recent income tax laws have been passed took effect February 25, 1913. The revenue

acts thereunder are based on the assumption that March 1, 1913, was the effective date of the amendment.

The Revenue Act of 1913 taxed income for 1913 from March 1st to December 31st, and for calendar years thereafter. This act allowed deductions "for losses actually sustained during the year," but did not specifically indicate the basis of the loss.

The Revenue Act of 1916 provided as follows as to losses by individuals:

> "Sec. 5. * * * (a) * * * Fourth. * * * *Provided,* That for the purpose of ascertaining the loss sustained from the sale or other disposition of property, real, personal, or mixed, acquired before March first, nineteen hundred and thirteen, the fair market price or value of such property as of March first, nineteen hundred and thirteen, shall be the basis for determining the amount of such loss sustained;"

Regulations 33 (Revised), Treasury Decision 2690 promulgated January 2, 1918, construing the Revenue Act of 1916, contained the following provisions:

> "Art. 147. In the case of the sale of assets—real, personal, or mixed—the loss will be the difference between the cost thereof, or the value as of March 1, 1913, if acquired before that date, and the price at which disposed of. * * * "

Treasury decision 2740 issued June 24, 1918, contained the following:

> "In order to determine *whether there has been gain or loss on a sale*, and the amount of the gain, if any, in general under all three acts [the Acts

of 1909, 1913 and 1916] an amount must be withdrawn from the gross proceeds sufficient to restore the cost of the property or the capital value that existed at the commencement of the period under consideration (either January 1, 1909, or March 1, 1913)." (Italics ours.)*

Thus when the Revenue Act of 1918 was enacted in February, 1919, the holding of the Commissioner of Internal Revenue was that the original cost of property acquired prior to March 1, 1913, was immaterial in the case of individuals and that losses were to be determined by deducting the sale price from the March 1, 1913, value.

The Contemporaneous Construction of the Revenue Act of 1918 by the Officials Charged with its Enforcement was that Losses Sustained by the Sale of Property Acquired Prior to March 1, 1913, should be Based on the March 1, 1913, Value.

After the approval of the Revenue Act of 1918 on February 24, 1919, Regulations 45 were promulgated by the Commissioner of Internal Revenue and approved by the Secretary of the Treasury April 16, 1919 (Treasury Decision 2831), which provided:

"Article 1561. * * * For the purpose of ascertaining the gain or loss from the sale or exchange of property the basis is (a) its fair market price or value as of March 1, 1913, if acquired prior thereto, or (b), if acquired on or after that date, its cost or its approved inventory value. * * *"

*The reference to January 1, 1909, is applicable only to the case of corporations, which were first taxed on income under the Revenue Act of 1909, which, as has been stated, was sustained as an excise tax.

This regulation remained in effect during the years 1919 and 1920. During the time the regulation was in effect James J. Flannery sustained the loss involved in this suit and his executors filed the return for the year 1919. It was not until July 28, 1921, that by Treasury Decision 3206, Article 1561 of Regulations 45 was amended so as to deprive tax-payers of the right to take losses based on March 1, 1913, values.

The tax involved in this suit was assessed under this amendment to the regulations, retroactively applied.

It is submitted that the immediate and contemporaneous construction of the Revenue Act of 1918 by the officials charged with its enforcement is of far greater weight than a regulation promulgated more than two years after the passage of the act.

The Allowance of a Loss Based on March 1, 1913, Value in the Case of Property Acquired before that Date Accords with Other Provisions of the Revenue Act of 1918 and with Decisions of the United States Supreme Court as to Capital and Income.

The provisions of the Act which are before the Court in this case provide for deductions from income earned during the year to provide for losses of assets. But assets are wasted in other ways than by losses. And provision must be made for deductions on such accounts. For instance, provision is made in the Act for the waste caused by depreciation of buildings, machinery, etc., and by depletion of natural resources. If the argument of the Solicitor General in this case

is sound then the deductions from income to cover losses due to depreciation and depletion must be based on cost and not on March 1, 1913, value. But such is not the case.

Section 214 (a) 10, of the Revenue Act of 1918 provides that in the case of properties acquired prior to March 1, 1913, the fair market value of the property on that date shall be taken in lieu of cost in determining a reasonable allowance for depletion and depreciation of improvements in the case of mines, oil and gas wells, and other natural deposits and timber.

Regulations 45, Article 161, relating to depreciation, states:

> * * * "The proper allowance for such depreciation of any property used in the trade or business is that amount which should be set aside for the taxable year in accordance with a consistent plan by which the aggregate of such amounts for the useful life of the property in the business will suffice, with the salvage value, at the end of such useful life to provide in place of the property its cost, or *its value as of March 1, 1913, if acquired by the taxpayer before that date.* * * *"

These statutory provisions and Departmental regulations show a consistent recognition of the underlying theory that all property on hand as of March 1, 1913, was capital and that only acquisitions since that time constituted income. It follows that depreciation or depletion was measured in such a way that the capital on hand March 1, 1913, would be returned to the taxpayer, and deductions were allowed in such a way as to recognize that the capital on hand March 1, 1913, was what had been lost.

This same principle had been stated and applied by the United States Supreme Court in early cases, as follows:

> * * * "In order to determine whether there has been gain or loss, and the amount of gain, if any, we must withdraw from the gross proceeds an amount sufficient to restore the capital value that existed at the commencement of the period under consideration. * * *
>
> "When the act took effect, plaintiff's timber lands, with whatever value they then possessed, were a part of its capital assets, and subsequent change of form by conversion into money did not change the essence. * * *" (Doyle v. Mitchell Brothers Company, 247 U. S. 179, 185, 187.)

> * * * "Certainly the term 'income' has no broader meaning in the 1913 Act than in that of 1909 * * * and for the present purpose we assume there is no difference in its meaning as used in the two acts. This being so, we are bound to consider the accumulations that accrued to a corporation prior to January* 1, 1913, as being capital, not income, for the purposes of the act. And we perceive no adequate ground for a distinction, in this regard, between an accumulation of surplus earnings, and the *increment due to an appreciation in value of the assets of the taxpayer.*" (Southern Pacific Co. v. Lowe, 247 U. S. 330, 335.) (Italics ours.)

It is apparent from the foregoing that the provisions of the Revenue Act of 1918, that statutory loss is to be determined by the value of the property on March

*Apparently the court referred to January 1, 1913, instead of March 1, 1913, because in the particular case the accumulations were wholly prior to January 1, 1913. There was no apparent intention to make any date other than March 1, 1913, the controlling one.

1, 1913, even if that is in excess of cost, are consistent with the general theory of the revenue acts in respect to questions relating to capital and income, that the value of the property as of March 1, 1913, is to be considered as the taxpayer's investment therein.

The Enforcement of a Retroactive Regulation Should Be Avoided.

It should be particularly noted that when James J. Flannery sold the stock of the Flannery Bolt Company in October, 1919, under the then existing regulation it was perfectly clear that he had sustained a loss which could be deducted from his gross income in determining net income. As a matter of fact the same regulation was in effect when the executors made the return for the year 1919.

When James J. Flannery took the loss he had a right to think that he could sell his stock and deduct the loss from income. He and other taxpayers who may have taken such losses, which they expected to offset against gains from other stock that they sold, are in the position of being trapped by the change in the regulations. It is obvious that many taxpayers in the position of Mr. Flannery took other gains in 1919 which they thought would be offset by losses. By the retroactive change in the regulations their gains may be taxable but their losses not deductible. While we do not know whether or not this was the case with James J. Flannery, it should be pointed out as a strong possibility in the case of any taxpayer, and as a reason for not changing the regulations retroactively. The policy to be adopted toward retroactive changes in the

regulations is indicated by Section 1008 of the Act of 1924, which only permits retroactive changes immediately required by a decision of a court.

The return of the executors was correct when made, *according to the law and regulations then existing.* They made no error at all in the return. Why should an additional tax have been assessed?

The Amendment to Article 1561 of Regulations 45, Under which the Tax was Assessed, was Due to a Mistaken Interpretation of the Case of Goodrich v. Edwards, 255 U. S. 527.

The case of Goodrich v. Edwards, 255 U. S. 527, was decided by the Supreme Court of the United States March 28, 1921. The principal point involved in that case and in a group of cases decided the same day was that profits realized upon the sale of property constituted income and that so much of it as accrued after March 1, 1913, was taxable under the income tax laws of 1916 and 1917 and the Sixteenth Amendment. It had been contended by taxpayers that the total amount realized from the sale of property was capital as distinguished from income, being an increment in value of the property while owned and held, and therefore no part thereof could be taxable as income. This question which had for a long time been the subject of debate among persons interested in taxation was finally settled by the definite decision that such gains constituted income, in the four cases of Merchants Loan & Trust Co. v. Smietanka, 255 U. S. 509 (sale of stock held by a trustee); Eldorado Coal Co. v. Mager, 255 U. S. 522 (sale of its mine by mining company); Good-

rich v. Edwards, 255 U. S. 527 (sale of stock held as investment); and Walsh v. Brewster, 255 U. S. 536 (sale of bonds held as investment).

In the case of Goodrich vs. Edwards there was a second point: The plaintiff had acquired certain stock in 1912 at a cost of $291,600. On March 1, 1913, the value of this stock was $148,635.50. It was sold in 1916 for $269,346.25. Thus the price at which it was sold showed a loss on the transaction taken as a whole but a profit compared with the March 1, 1913, value. A tax had been collected on a gain measured by the difference between the March 1, 1913, value and the sale price.*

This case is an unsatisfactory one, in that the Solicitor General did not attempt to defend the action of the Bureau of Internal Revenue. He confessed error with respect to the assessment, stating that in his opinion the statute imposed a tax upon a sale of property only where there was a gain over the original price paid (255 U. S. 533, 534). There was therefore no argument on the effect of the March 1, 1913, value as determining gain.

This court in its opinion pointed out that the Revenue Act of 1916 taxed as income "gains * * * derived from * * * sales or dealings in property"; that the court in *Eisner v. Macomber*, 252 U. S. 189, 207, defined income as " 'the gain derived from capital, from labor, or from both combined' provided it be understood to include profit gained through a sale or conversion of capital assets;" and then concluded that no gain—

*Walsh v. Brewster is similar to Goodrich v. Edwards and is cited as authority for the Government's position. It is not discussed in this brief because the opinion simply refers to and follows Goodrich v. Edwards. What is said in this brief, therefore, as to Goodrich v. Edwards is equally applicable to Walsh v. Brewster.

and hence no taxable income—was realized upon this sale.

The court thus held that the phrase "gains derived from sales or dealings in property" in the Revenue Act of 1916 meant "profit gained through a sale or conversion of capital assets," which was the only kind of gain from such a transaction which the court had included in its definition of income taxable under the Sixteenth Amendment in *Eisner v. Macomber*. This construction of the phrase was acquiesced in by the Solicitor General. To have widened the scope of the phrase to include a sale where there was no *profit* would have raised a grave constitutional doubt as to whether such "gains" were income within the meaning of the Sixteenth Amendment as construed by the court. Indeed, the Solicitor General admitted this on page 59 of his brief in that case.

The case of Goodrich v. Edwards did not involve the deductibility of losses. The facts did not raise any such questions. Losses were not mentioned. The reasoning of the decision has no bearing whatever on the deductibility of losses.

Manifestly the right to tax income and the right to authorize deductions are governed by different principles. For while, under the Sixteenth Amendment, Congress cannot tax as "income" anything which the courts do not hold is "income," it may allow many deductions from gross income in determining net income which are wholly in the discretion of Congress—which may, indeed, be pure acts of grace on its part—so long as the statute applies with geographical uniformity throughout the United States. *Brushaber v. Union Pacific Ry. Co.*, 240 U. S. 1.

While it may be true that certain deductions from

gross income *must* be allowed, Congress may and did in the Revenue Act of 1918 allow many deductions from gross income in determining net taxable income which are *not* necessary or even proper in a determination of net income from an economic point of view. Thus individuals are allowed to deduct contributions to religious, charitable, scientific, or educational corporations, up to a specified extent (Sec. 214 (a) (11)), interest and taxes on personal as well as on business obligations and property (Sec. 214 (a) 2, 3), and losses even though "*not* connected with trade or business * * * if arising from fire * * * or other casualty" (Sec. 214 (a) 6). A personal exemption—which for practical purposes amounts to a deduction—is allowed; credits or exemptions are allowed for dependents. These are pure acts of grace on the part of Congress.

A similar act of grace is the provision in Section 213 (b) 8 that so much of the compensation received from the government by a person in the army or navy during the late war as does not exceed $3,500 need not be included in gross income.

Congress need not have permitted any of the deductions mentioned above. However, in its discretion it chose to do so. Similarly it chose to permit the taxpayer to take as a deduction losses based on March 1, 1913, value. It took away that privilege in the 1921 Act. It restored it in the 1924 Act. None of the considerations affecting deductions for losses which Congress may in its discretion permit has any bearing upon the question of what is included in the definition of income as that word is used in the Sixteenth Amendment. But it was this latter question which was under consideration in the Goodrich case. Neither the decision in that case nor the opinion throw any

light on the problem here presented which is whether or not Congress did intend to permit taxpayers to deduct losses based on the March 1, 1913, value.

The Court of Claims in deciding this case below dismissed the Government's argument based upon the Goodrich case without difficulty. The court said:

> "It is urged, however, that the cases of *Goodrich v. Edwards*, 255 U. S. 527, and *Walsh v. Brewster*, 255 U. S. 536, are decisive of the question. These cases deal with the question of 'gain' in the act of 1916. They do not discuss or decide whether a loss claimed and ascertained as in this case is a proper deduction in computing net income of the individual under the revenue act of 1918. That the right to tax income and the right to authorize deductions are governed by different considerations is manifest. Our conclusion is that the plaintiffs are entitled to recover." * * *

In the case of Ludington v. McCaughan, 1 Fed. (2d) 689, the Circuit Court of Appeals for the Third Circuit decided under the Revenue Act of 1918 that where property acquired prior to March 1, 1913, at a price less than the fair market value on that date is sold by a taxpayer a loss may be deducted based on the March 1, 1913, value. This opinion contains such a convincing statement of the law that we should like to quote it in full were it not for the limitation of space. The court discussed the Goodrich and Walsh cases and said:

> "While in the language of the statute in respect to a taxable gain derived from the sale of personal property there was manifestly a constitutional question, no such question can be found in its language in respect to a loss which the statute

authorizes the taxpayer to deduct in ascertaining taxable incomes. No mention of losses is made in the Sixteenth Amendment, and there is no constitutional limitation upon the power of Congress in respect to the allowance of losses. Congress may allow or disallow them at will and upon any basis. Taxable gain is a constitutional concept denoting income which the taxpayer has derived, while deductible loss is a creation of Congress, varying from time to time as Congress deals with it in different ways.

"Reading the decisions of the Supreme Court in the Goodrich and Walsh cases as interpretations of the law only with reference to taxable gains—the subject of deductible losses was not touched—and believing that Congress is free to make its own definition of deductible losses, it follows that in construing the provision with reference to 'loss sustained' here in question, there is no constitutional limitation to be enforced and no constitutional doubt to be avoided, and hence no reason for restricted construction or for any construction which fails to give the words of the statute their plain meaning and import. *United States* v. *Standard Brewery Co.*, 251 U. S. 210, 217; *MacKenzie* v. *Hare*, 239 U. S. 299, 308; *Caminetti* v. *United States*, 242 U. S. 470, 485; *Russell Motor Car Co.*, v. *United States*, 261 U. S. 514, 519.

* * * * * * *

"Feeling that in this regard the power of Congress was not limited, we are constrained to construe the words 'loss sustained' in the section in question literally and to hold that they mean just what they say, even though, as in this instance, the loss sustained, ascertained in the manner prescribed by statute, is greater in figures than it is in money, and the effect of its deduction from gross income is to decrease net income below its actual level.

> "We are driven to this conclusion, startling as it may seem, because we cannot hold that Congress did not mean what it said, and also because the language of a statute being plain and its meaning clear, and the statute itself being within the constitutional authority of the law-making body which passed it, our sole function is to enforce the law according to its terms. *Lake Co.* v. *Rollins*, 130 U. S. 662, 670, 671; *Caminetti* v. *United States*, 242 U. S. 470, 485."

There is a decision of the United States District Court for the Northern District of California, which holds the same thing: Vance v. McLaughlin, which is not in the Federal Reporter but which can be found in Commerce Clearing House Unabridged Federal Income Tax Service 1924, Volume 2, page 1296.

It is, therefore, confidently asserted that the Goodrich case which arose under the 1916 Act and which concerned the question of what is included in the term "income" in the Sixteenth Amendment, has no bearing on the case at bar which arose under the 1918 Act and involves only an inquiry as to what deductions for losses Congress intended to permit.

If there is any Doubt as to the Interpretation of the Revenue Act of 1918, it Should be Resolved in Favor of the Taxpayer.

As to this it is sufficient to point to the long-established rule of construction:

> "In the interpretation of statutes levying taxes it is the established rule not to extend their pro-

visions, by implication, beyond the clear import of the language used or to enlarge their operations as to embrace matters not specifically pointed out. In case of doubt they are construed most strongly against the Government, and in favor of the citizen. United States *v.* Wigglesworth, 2 Story 369; American Net and Twine Company *v.* Worthington, 141 U. S. 468, 474; Benzinger *v.* United States, 192 U. S. 38, 55."

(Gould *v.* Gould, 245 U. S. 151.)

Conclusion.

It is respectfully submitted that under the provisions of the Revenue Act of 1918, according to the natural meaning of the words of the act, the long-established administrative practice under previous acts, the contemporaneous construction of the act by the Bureau of Internal Revenue after its passage, and consistently with the other provisions of the act and Supreme Court decisions, a taxpayer might deduct as a loss in the year 1919 the difference between the March 1, 1913, value of property acquired by him prior to that date and its sale price in 1919 in spite of the fact that such sale price was more than the original cost prior to March 1, 1913.

It is further submitted that there is nothing in the case of Goodrich *v.* Edwards, 255 U. S. 527, or in Walsh *v.* Brewster, 255 U. S. 536, inconsistent with this view, those cases involving the construction of a different statute and involving the question of gains which have constitutional considerations not applicable to losses.

It is therefore respectfully submitted that the judgment of the Court of Claims should be affirmed.

EDWARD B. BURLING,
SPENCER GORDON,
Attorneys for Appellees.

Acts of 1917 and 1916.

(No provision as to ascertaining gain or loss on sale of property acquired on or after March 1, 1913.)

Sec. 2. (c) For the purpose of ascertaining the gain derived from the sale or other disposition of property, real, personal, or mixed, acquired before March first, nineteen hundred and thirteen, the fair market price or value of such property as of March first, nineteen hundred and thirteen, shall be the basis for determining the amount of such gain derived.

Sec. 5. Fourth. (2) *Provided*, That for the purpose of ascertaining the loss sustained from the sale or other disposition of property, real, personal, or mixed, acquired before March first, nineteen hundred and thirteen, the fair market price or value of such property as of March first, nineteen hundred and thirteen, shall be the basis for determining the amount of such loss sustained;

Act of 1918.

SEC. 202. (a) THAT FOR THE PURPOSE OF ASCERTAINING THE GAIN DERIVED OR LOSS SUSTAINED FROM THE SALE OR OTHER DISPOSITION OF PROPERTY, REAL, PERSONAL, OR MIXED, THE BASIS SHALL BE—

(1) IN THE CASE OF PROPERTY ACQUIRED BEFORE MARCH 1, 1913, THE FAIR MARKET PRICE OR VALUE OF SUCH PROPERTY AS OF THAT DATE; AND

(2) IN THE CASE OF PROPERTY ACQUIRED ON OR AFTER THAT DATE, THE COST THEREOF; OR THE INVENTORY VALUE, IF THE INVENTORY IS MADE IN ACCORDANCE WITH SECTION 203.

Mr. Beck says no change intended.

Act of 1921.

Sec. 202. (a) That the basis for ascertaining the gain derived or loss sustained from a sale or other disposition of property, real, personal, or mixed, acquired after February 28, 1913, shall be the cost of such property; * * *

(b) That basis for ascertaining the gain derived or loss sustained from the sale or other disposition of property, real, personal, or mixed, acquired before March 1, 1913, shall be the same as that provided by subdivision (a); but—

(1) If its fair market price or value as of March 1, 1913, is in excess of such basis, the gain to be included in the gross income shall be the excess of the amount realized therefor over such fair market price or value;

(2) If its fair market price or value as of March 1, 1913, is lower than such basis, the deductible loss is the excess of the fair market price or value as of March 1, 1913, over the amount realized therefor; and

(3) If the amount realized therefor is more than such basis but not more than its fair market price or value as of March 1, 1913, or less than such basis but not less than such fair market price or value, no gain shall be included in and no loss deducted from the gross income.

Act of 1924.

Sec. 204. (11). (b). The basis for determining the gain or loss from the sale or other disposition of property acquired before March 1, 1913, shall be (a) the cost of such property (or, in the case of such property as is described in paragraph (1), (4), or (5), of subdivision (a), the basis as therein provided), or (B) the fair market value of such property as of March 1, 1913, whichever is greater. * * *

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No. 527.

IN THE

Supreme Court of the United States.

OCTOBER TERM, 1924.

APPEAL FROM THE COURT OF CLAIMS.

THE UNITED STATES, Appellant,

vs.

HARRIET ROGERS FLANNERY and J. ROGERS FLANNERY, Executors of the Estate of JAMES J. FLANNERY, Deceased.

PETITION FOR A REHEARING.

TO THE HONORABLE THE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

Harriet Rogers Flannery and J. Rogers Flannery, Executors of the Estate of James J. Flannery, Deceased, your petitioners, respectfully submit that they have been aggrieved by the opinion of the Honorable Justices of this Court rendered herein on the 13th day of April, 1925,

in the respects herein set forth, and pray for a rehearing of said matter.

1. The opinion errs in holding that your petitioners' decedent sustained no actual loss in the transaction in question because said decedent sold his stock for more than the original cost thereof; and

2. In holding that the Court's decision reached in this case is controlled and required by the decisions of this Court in

Goodrich *v.* Edwards, 255 U. S. 527, and
Walsh *v.* Brewster, 255 U. S. 536.

POINT 1.

Accumulations prior to March 1, 1913, are capital. Under our system of law it is the property itself and not the original cost of it to which the owner is entitled. A capital accumulation in property prior to March 1, 1913, even though not resulting from money expenditure, is a property right and a subsequent sale at a price less than original cost plus subsequent accumulations prior to March 1, 1913, is an actual loss.

POINT 2.

The rule adopted in Goodrich *v.* Edwards, *supra,* and Walsh *v.* Brewster, *supra,* require that the loss resulting from the subsequent sale of property acquired prior to March 1, 1913, should be on the basis of cost or market, whichever is higher, and not on the basis of cost or market, whichever is lower. The Revenue Act of 1924 has adopted the correct basis. The interests of the taxpayer require this construction, which results in no appreciable loss to the Treasury.

POINT 1. Accumulations prior to March 1, 1913, are capital. Under our system of law it is the property itself and not the original cost of it to which the owner is entitled. A capital accumulation in property prior to March 1, 1913, even though not resulting from money expenditure, is a property right and a subsequent sale at a price less than original cost plus subsequent accumulations prior to March 1, 1913, is an actual loss.

All accumulations of income, including the increment due to appreciation in value of the assets of the taxpayer prior to March 1, 1913, are capital for the purposes of the Federal Revenue Laws.

> Southern Pacific Company *v.* Lowe, 247 U. S. 330.

where the court disposes of this question in these words:

> "This being so, we are bound to consider accumulations that accrued to a corporation prior to January 1, 1913, as being capital, not income, for the purposes of the act. And we perceive no adequate ground for a distinction in this regard, between an accumulation of surplus earnings, and the increment due to an appreciation in value of the assets of the taxpayer."

This court has always held that it is the property itself and not the original cost of it to which the owner is entitled.

> Minnesota Rate Cases, 230 U. S. 350,

where the court, at page 454, declared the principle in these words:

> "It is clear that in ascertaining the present value we are not limited to the consideration of the amount of the actual investment. If that has been reckless

> or improvident, losses may be sustained which the community does not underwrite. As the company may not be protected in its actual investment, if the value of its property be plainly less, so the making of a just return for the use of the property involves the recognition of its fair value if it be more than its cost. The property is held in private ownership, and it is that property, and not the original cost of it, of which the owner may not be deprived without due process of law."

To be sure, this was a confiscation case, but it is difficult to distinguish between property rights which may be taken in the form of rate regulation and property rights which may be appropriated under a rate of taxation which in 1918 amounted to 12% normal tax and up to 65% surtax, and which in 1919, the year in question, amounted to a normal tax of 8% and a surtax up to 65%. This principle that it is the present value of the property and not the original cost thereof to which the owner is entitled is settled by this court in an unbroken line of confiscation and condemnation cases, and in the Minnesota Rate Cases just cited is regarded as so thoroughly established as not to require the citation of authorities.

Our income tax laws might have been drawn on the theory that capital gains should not be considered as a part of gross income subject to taxes, but it is well known that Congress has adopted a different policy and included capital gains in gross income subject to income taxes. The rate of tax upon capital gains was the same as the rate upon other income, until the enactment of the Revenue Act of 1921, which established a maximum 12½% rate where the property had been held in excess of two years. Just as capital gains were included in gross income, so capital losses were allowed as a deduction from gross income in determining net taxable income, and this practice is uniform throughout all our revenue laws beginning with the Revenue Act of 1913, except that the

Revenue Act of 1913 limited deductions for losses to those incurred in trade or arising from fires, storms, or shipwreck, and not compensated for by insurance or otherwise. The Revenue Act of 1916 extended the provisions for deductions for losses to include losses in transactions entered into for profit but not connected with trade or business up to the amount of the profits arising therefrom. Finally, in the Revenue Act of 1918, the basis of determining gain or loss sustained from the sale or other disposition of property are made identical and are provided for in the same words (see Section 202, Revenue Act of 1918).

Under the interpretation of this section 202 of the Revenue Act of 1918 adopted in the opinion in this case, the deduction for losses is confined to the difference between the original cost or market value on March 1, 1913, whichever is lower, and the selling price.

If the property were seized in condemnation proceedings on March 1, 1913, it is the present value of the property and not the original cost of it to which the owner would be entitled. If the property, on March 1, 1913, had been sold at its then market value to a purchaser who in 1919 sold the same property at a loss, the purchaser would be entitled to deduct such loss in computing net taxable income of the year in question. If, however, the original purchaser of the property does not sell on March 1, 1913, but continues to hold the property and himself takes a loss in the year in question, then the loss (above the original cost) is denied to the holder.

As it is the present value of the property itself and not the original cost of the property to which the owner is entitled under our system of law, it is difficult to understand the basis for allowing a full deduction to a purchaser from an owner on March 1, 1913, at the then market value, but to deny a deduction to such owner

who himself continued to hold the same property and later sold it for less than such value, even though above original cost.

Doubtless the view of the court was influenced by the fact that the market value of stock fluctuates irrespective of the intrinsic value of the stock, but it is also a well-known fact that in many cases the appreciation in market value of stocks is due to an accumulation of corporate surplus. Appreciation in price of securities may be due to the external conditions of an improved market, or may be due to an enhancement in intrinsic worth resulting from the accumulation of surpluses which might have been paid in dividends. It seems unfair as between taxpayers to allow a stockholder in the corporation which has made a practice of distributing all of its surplus in dividends from the date of original purchase prior to March 1, 1913, down to that date to get the benefit of all such dividends without income taxation, and on subsequent sale to tax a stockholder upon such surpluses in the corporation which has allowed its surpluses to accumulate over the same period. If the enhancement in market value of the security prior to March 1, 1913, above the original cost due to the accumulation of such surplus is to be ignored in determining the deductible loss upon sale, the substance of the transaction is a capital tax, not an income tax. To be sure, we are dealing with deductions and it is for Congress to say to what extent deductions from gross income should be allowed in determining net taxable income. The law purports to allow a deduction for capital losses, and this court has decided that accumulations prior to March 1, 1913, are capital and not income.

When consideration is given to the cases which arise with regard to property other than securities, it at once bceomes apparent that a taxpayer may suffer an actual

and severe loss even though the price realized may be above original cost. Some of the instances are as follows:

(*a*) A copartnership begins business 50 years prior to March 1, 1913, and through industry, skill, integrity, close attention to business and a long and unbroken course of fair dealing, builds up a good will of admitted great value on March 1, 1913. Such firm is engaged in a world-wide mercantile business which during the world war and the reconstruction period following the war is practically wiped out and sells its entire business with little or no allowance for good will. The good will may have had an actual value of $1,000,000 on March 1, 1913, but the firm is unable to prove any actual original cost thereof in money. To be sure a half dozen lives may have been devoted to the service and effort which built up this good will, but there is no actual cash outlay. Can it be said that a firm which in 1919 sells its good will, built up through 50 years of effort and which on March 1, 1913, could have been readily sold for $1,000,000 or more, suffers no actual loss by the disposal of such good will for a nominal amount in 1919 or 1920?

(*b*) A manufacturing corporation is formed by consolidations of other existing companies late in the last century and in that connection takes over from them very large holdings of timber lands at a small original cost. The timber continues to grow and on March 1, 1913, is of great value. Subsequently, in 1918 to 1920, the spruce bud-worm ravages the forest and destroys millions of dollars worth of spruce trees valuable for pulp wood or lumber. Is the loss for income tax purposes to be measured by the original cost of a half century ago and without allowing for the increase in value due to growth as well as the appreciation in price?

(*c*) A man personally plants an orchard 40 years ago and spends all his intervening time in tending and

caring for the orchard, until on March 1, 1913, such orchard is in its prime. If the orchard should be destroyed by a cyclone in 1918, 1919 or 1920, can it be said that the owner has suffered no loss merely because he has no cash outlay? In this latter case, assuming that the owner had devoted all of his time to the orchard, he would be able to prove the value of the labor that had gone into the orchard. This, however, would be but a small portion of the actual expenditure, for the thing that makes success is the skill, care and devoted attention which cannot be measured in money. One man spent a lifetime with nothing to show for it at the end. Another, under apparently similar external circumstances, but with a different character, makes a great success. Who is qualified to measure in money the added value of the successful labor over that of the man who failed?

Under the rule adopted by the court, the taxpayer will be denied all deduction for losses upon the sale of property acquired prior to March 1, 1913, unless the taxpayer is in a position to prove the original cost of the investment. During the period prior to the revenue laws it was well known that accounting had not reached its present state of exactness and many records which were sufficient for the purpose of ordinary business operations were wholly defective in disclosing the original cost of capital assets.

POINT 2. The rule adopted in Goodrich *v.* Edwards, *supra,* and Walsh *v.* Brewster, *supra,* requires that the loss resulting from the subsequent sale of property acquired prior to March 1, 1913, should be on the basis of cost or market, whichever is higher, and not on the basis of cost or market, whichever is lower. The Revenue Act of 1924 has adopted the correct basis. The interests of the taxpayer require this construction, which results in no appreciable loss to the Treasury.

The cases of Goodrich *v.* Edwards, *supra,* and Walsh *v.* Brewster, *supra,* do not require the denial of a deduction based on the market value on March 1, 1913, when above original cost. Those two cases were decided to relieve a taxpayer from tax where the sale price was below the actual investment. It was a generous and proper interpretation of the statute not to reflect a heavy tax where in fact there was no gain on the basis of the outlay; but it does not follow that another taxpayer should be subjected to equally heavy taxes without allowing for a loss based upon the value of the property at the time the Sixteenth Amendment was enacted and the first income tax law thereunder became effective. There is just as much equity in allowing a loser a deduction based upon the original cost or the value on March 1, 1913, whichever is higher, as there is in determining the gains on this basis, and the wisdom of this course is indicated by the action of Congress on the recommendation of the Treasury Department in embodying such provision in the Revenue Act of 1924, after three years experience under the Revenue Act of 1921 in limiting the deduction to original cost or market value on March 1, 1913, whichever is lower. There is no case of greater hardship upon the taxpayer than to impose the very heavy normal and

surtax rates in effect in 1918 and 1919 without allowing a deduction for losses based upon capital values as of March 1, 1913, when the Sixteenth Amendment took effect, and these cases of great individual hardship can be avoided without appreciable loss to the Treasury. Congress recognized all this in enacting the Revenue Act of 1924, for the report of the Ways and Means Committee, in reporting that Act back to the House with the recommendation that it pass, contained a provision which referred to the section in question in these words:

> "(8) Subdivision (*b*) provides that the basis for determining the gain or loss from the sale or other disposition of property acquired before March 1, 1913, shall be the cost of the property or its fair market value as of March 1, 1913, whichever is higher. This provision changes the existing law in the interests of the taxpayer. It simplifies exceedingly the rule in effect under the present law without appreciable loss to the Treasury." (Report of Ways and Means Committee, p. 18.)

Conclusion.

Section 202 of the Revenue Act of 1918 provides the basis for the determination of gain or loss in identical words. The cases of Goodrich *v.* Edwards, *supra,* and Walsh *v.* Brewster, *supra,* require an identical and not a correlative interpretation. The interests of the taxpayer, so fully protected by the court in those cases, require that the burdensome tax rates in effect in 1918 and 1919 shall not be imposed without allowing a deduction for losses on the basis of capital values existing on March 1, 1913, even though above original cost, and this can be done without appreciable loss to the Treasury, as Congress and the Treasury have ascertained after a test of the other rule in the Revenue Act of 1921.

WHEREFORE, petitioner respectfully urges that a rehearing may be granted and that the mandate of this court may be stayed pending the disposition of this petition.

Dated: New York, N. Y., May 15, 1925.

HARRIET ROGERS FLANNERY and
J. ROGERS FLANNERY, Executors of the Estate of JAMES J. FLANNERY, Deceased.

By
SANFORD ROBINSON,
Attorney for Respondent.

I, SANFORD ROBINSON, of New York, N. Y., an attorney regularly admitted to practice in the Supreme Court of the United States, do certify that in my opinion the foregoing petition for rehearing in the case of The United States, Appellant, *v.* Harriet Rogers Flannery and J. Rogers Flannery, Executors of the Estate of James J. Flannery, Deceased, No. 527, is well founded and that it is presented in good faith and not for the purpose of creating a delay.

SANFORD ROBINSON

Supreme Court of the United States.

OCTOBER TERM, 1924.

No. C 1080.

THE UNITED STATES OF AMERICA,
APPELLANT,
v.
HARRIET R. FLANNERY,
RESPONDENT.

Brief Submitted by Richard W. Hale and Reginald H. Smith, Amici Curiae.

INTRODUCTION.

This brief is filed for the purpose of commenting upon certain aspects of the case of—

Goodrich v. *Edwards*, 255 U.S. 527 (1921).

If the case now at bar is to be considered *de novo*, that is one thing. In that event the contentions upon either side must stand or fall because of their inherent soundness, and not because *Goodrich* v. *Edwards* rules as a precedent. On the other hand, if this case is to be considered from the point of view of putting *Goodrich* v. *Edwards* into one pan of the scales of justice as a thing of weight—why then there is occasion to

weigh it carefully, and upon that matter we attempt to make a contribution.

ARGUMENT.

The sum and substance of what we have to say is that the extraordinary complications of our present generation strike at the root of our system of reliance upon precedents. Times are changing in the law, and in the present time a precedent is a valuable thing only when it results from a controversy wholly and fairly fought out. The adversaries must have been properly matched and fairly confronted. They must have desired to win, and they must have been well armed and equipped to that end.

Goodrich v. *Edwards* is quite the reverse of all this. The Goodrich case was one between the government and a single taxpayer. The taxpayer was not a fair representative of the whole body of interested persons opposed to the government. It is probable that the government wanted him to win *in the way he did* as badly as he wanted to win, no matter what way. At any rate there was a large body of interested persons whom the government did defeat by that decision, if the construction given it by the taxing authorities is correct. It is probable that there was a distinct intention and hope to defeat this particular class of persons in their absence, and without a hearing. Their first appearance before this Court is in this and the parallel cases now pending here. Under such circumstances they ought not to be prejudiced by the previous decision.

If we were dealing with an isolated case, there might be some argument in favor of standing by the old

customs for convenience and general advantage. The power to rely upon precedents is a valuable one, and high authority for precedent is a thing which has many advantages. But this is not an isolated case. Far from being sporadic or unusual, the trouble is almost epidemic, and there is a general situation which should be faced.

We purpose to illustrate and describe this situation by stating a number of actual or reasonably imagined analogous cases.

Take, first, cases in which a will is construed and other like equity suits. In these it is trite that the Court will insist on hearing argument from all classes in interest.

On the other hand, illustrating the same point, take the declaratory opinions such as those that are given by the justices of the Supreme Judicial Court of Massachusetts "upon important questions of law and upon solemn occasions." There is an outstanding warning that these opinions are substantially not binding as precedents for lack of argument in behalf of those interested.

> "These opinions, as has been decided repeatedly, are purely advisory, are given without the benefit of argument, and are formed and expressed under such circumstances that they cannot be considered as binding authorities and are open to reconsideration and revision. They, however, presuppose 'that the subject to which' they relate has 'been judicially examined and considered.' The justices, when called upon, sitting as a court, to deal with such questions again, regard it as their 'duty

> most sedulously to guard against any influence which might flow from . . . previous consideration' of the same questions in their advisory capacity."
>
> *Perkins* v. *Westwood,* 226 Mass. 268, at 271 (1917).

Next take the story which we hang, as upon a peg, to the case of *United States* v. *Phellis,* 257 U.S. 156 (1921), although we do not suggest that it is the story of that case.

In the years 1913-1916 there were many reorganizations and consolidations. Afterwards the lawyers concerned realized that the exchanges made in some of these reorganizations registered a profit, brought about taxation of it and also started a new basis for fixing the profit upon a future sale. The matter usually comes up in a test case where a taxpayer appears to be resisting the tax on the exchange. But suppose a rich shareholder in the very Phellis case corporation had desired to sell his shares in 1918. If he had established a new basis of cost by the previous reorganization, he could afford to sell. If he had not done so, the tax on his profit would crush him. By the time the Phellis case was argued here anyone who had sold in 1918 must have been passionately desirous to see the government win the case and assess him for a 1915 tax.

We submit that it would be desirable and practicable for this Court to insist that such cases as the Phellis case should not be argued until the Court had before it briefs for the shareholders whose interest it was to lose the case, and for those whose interest was on the

contrary to win, and also until the Court knew which was which.

Next take the income-tax situation under the direct-tax clauses of the Constitution. The issue is clearly defined. On the one side, population; on the other side, constitutional foresight safeguarding the wealthier communities. In the Pollock arguments both sides were well represented, but in—

Springer v. *United States*, 102 U.S. 586 (1881)—

a Civil War income-tax case, the contestant who lost, with his professional income, was obviously not a fair representative of the property interests which the Constitution had sought to safeguard against mere population.

In the foregoing illustrations we have put before the Court a sufficient collection of instances. From them we may extract a principle that *stare decisis* does not apply when a question has been settled without full argument and without hearing both sides.

It remains to examine the question whether *Goodrich* v. *Edwards* is a case where this principle should be applied.

Who were the parties truly interested in the construction of the statute?

Goodrich and his ilk wanted to contend that he should not be taxed upon a gain when the amendment to the Constitution on March 1, 1913, found him owning securities which had sunk in value and the tax gatherer had figured the gain from that low point. If he could get rid of that tax, he cared not how.

The statute as it had been construed by regulations

did justice to men with losses, like Mr. Flannery. In 1913 his wealth was a question of fact. He was just as rich as he was in substance and he was made no richer by the circumstance that something had cost him more than it was then worth. He had property and it had value, but the incident that some of that property had been bought dear in the remote past was a trifle of little or no substantial importance. He was profoundly interested to contend that that trifle should not result in a heavy tax upon him. Accordingly Flannery sold the property at a substantial loss compared with its 1913 value. And he had been told by the tax gatherers in their regulations what the effect of that sale would be.

Goodrich and Flannery are really the contestants upon opposite sides of this controversy. It is true that the government stood to lose a lot of taxes on gains and to gain a lot of tax money by cutting down deductions for losses. The Department of Justice should have decided (and probably did decide) that there were more losses than gains to be affected by a decision in the Goodrich case. At any rate it allied itself with Goodrich in the sense that it endeavored to have him win upon a basis which would make the absent Flannery lose. But who warned Flannery?

If the Court will examine the record and briefs in the Goodrich case, it can satisfy itself that both were truly inadequate to a presentation of Flannery's contentions.

The important and almost crucial contention based on the regulations and practice of the Treasury was not open upon that record. But see—

National Lead Company v. *United States*,
252 U.S. 140, at 146 (1920)—

to the effect that that contention is ordinarily conclusive in favor of such men as Flannery.

The brief for Goodrich does not argue the case along statutory lines. The brief by the Solicitor General yields victory to Goodrich and then argues the statutory point. Goodrich files a reply brief and naturally does not even mention this or any of the weaknesses of a situation which is going to make Goodrich win.

CONCLUSION.

This is no sort of a case in which to apply the rule of *stare decisis*.

Richard W. Hale
RICHARD W. HALE.

Reginald H. Smith
REGINALD H. SMITH.

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IN THE

Supreme Court of the United States,

OCTOBER TERM, 1924.

UNITED STATES, Appellant, vs. HARRIET ROGERS FLANNERY, and J. ROGERS FLANNERY, executors of the estate of James J. Flannery, deceased.	No. 527.

BRIEF BY SANFORD ROBINSON, OFFICE AND POST OFFICE ADDRESS, NO. 26 LIBERTY STREET, NEW YORK, N. Y., AMICUS CURIAE.

Statement of Facts.

The respondents are the executors of the Estate of James J. Flannery, a taxpayer, now dead, who in 1919 sold certain shares of stock at a price which was less than the fair market value of said stock on March 1, 1913 but in excess of the actual original cost to him prior to March 1, 1913 of such shares. After the taxpayer died a return of net income subject to taxes under the Revenue Act of 1918 for the year 1919 was filed by his executors, in which a deduction was taken for a loss represent-

ing the difference between fair market value on March 1, 1913 and sales price in 1919 of such shares, but this deduction was disallowed by the Commissioner of Internal Revenue and an additional assessment based upon such disallowance was paid by the respondents who now seek to recover the amount of such additional assessment with interest.

Argument.

This case presents the question whether under the Revenue Act of 1918 a loss sustained from the sale of property acquired before March 1, 1913 shall be allowed as a deduction in computing net income for 1919 where such loss, within the terms of the statute, is the difference between the fair market value on March 1, 1913 of property acquired prior thereto and sales price thereof in 1919, and is incurred in trade or business or in a transaction entered into for profit when not connected with trade or business, although the sales price is in excess of the original cost of such property to the taxpayer. The provisions of the Revenue Act of 1918 effective for the year 1919, dealing with the basis of ascertaining gain or loss as applied to the deductions which are the subject of this suit, are clear and explicit in these words:

> "Section 214. (*a*) That in computing net income there shall be allowed as deductions:
>
> (4) Losses sustained during the taxable year and not compensated for by insurance or otherwise, if incurred in trade or business;
>
> (5) Losses sustained during the taxable year and not compensated for by insurance or otherwise, if incurred in any transaction entered into for profit, though not connected with the trade or business; * * *"

> "Section 202. (*a*) That for the purpose of ascertaining the gain derived or loss sustained from the sale or other disposition of property, real, personal, or mixed, the basis shall be—
>
> (1) In the case of property acquired before March 1, 1913, the fair market price or value of such property as of that date; and
>
> (2) In the case of property acquired on or after that date, the cost thereof; or the inventory value, if the inventory is made in accordance with Section 203."

The Revenue Act of 1918, like prior Federal Revenue laws, adopted the March 1, 1913 value as the basis for determining gains realized or losses sustained from the sale or other disposition of property acquired before March 1, 1913. The Revenue Act of 1918 was construed by the Treasury Department in Regulations 45, and Sections 214 and 202, *supra,* were interpreted in these words:

> "Article 1561. * * * For the purpose of ascertaining the gain or loss from the sale or exchange of property the basis is (*a*) its fair market price or value as of March 1, 1913, if acquired prior thereto, or (*b*), if acquired on or after that date, its cost or its approved inventory value. * * * ".

No question as to the meaning of the quoted sections of the statute was raised until the case of

> Goodrich *vs.* Edwards, 255 U. S. 527, decided March 28, 1921,

held in dealing with the question of gains that there was no taxable income unless the price realized was in excess of the original cost as well as in excess of the fair market value on March 1, 1913, upon the ground that there could be no income subject to

tax unless there was an actual profit. The Department of Justice concurred in this, and abandoned its former position in support of the tax in question in that case.

The Solicitor General stated in his brief for the Government in that case that the Treasury Department's construction of the Revenue Act of 1916 presented a "serious constitutional question". The court's decision is based on the construction of the statute and not on constitutional grounds. However, a court will construe a statute to avoid any question of constitutional limitations, where this is possible, and the court undoubtedly gave consideration to the Solicitor General's constitutional doubts.

There is no such constitutional question involved in the statutory provisions relating to allowable deductions in determining taxable net income, which is wholly a matter of the plain meaning of the statute, having in mind the familiar and established rule that a tax statute should be construed most strongly against the Government.

After Goodrich *vs.* Edwards, *supra,* was decided, Article 1561 of Regulations 45 was amended on July 28, 1921, by Treasury Decision 3206 to read in these words:

> "Article 1561. *Basis for determining gain or loss from sale.*—For the purpose of ascertaining the gain or loss from the sale or exchange of property the basis is the cost of such property, or if acquired on or after March 1, 1913, its cost or its approved inventory value. But in the case of property acquired before March 1, 1913, when its fair market value as of that date is in excess of its cost, the gain which is taxable is the excess of the amount realized therefor over such fair market value. Also in the case of property acquired before March 1,

> 1913, when its fair market value as of that date is lower than its cost, the deductible loss is the excess of such fair market value over the amount realized therefor. No gain or loss is recognized in the case of property sold or exchanged (*a*) at more than cost but at less than its fair market value as of March 1, 1913, or (*b*) at less than cost but at more than its fair market value as of March 1, 1913. * * *"

This amendment of Article 1561 is an attempt to shift to a taxpayer who sustains losses taxes which the Government may have lost by virtue of the decision in Goodrich *vs.* Edwards, *supra*, from taxpayers who had realized untaxed gains. There is no language in this decision which requires losses resulting from the sale of property acquired prior to March 1, 1913, to be determined on the basis of original cost or the value on March 1, 1913, whichever is lower. The question of statutory losses or the determination thereof was not before the court in this case. In fact Article 1561, as amended by Treasury Decision 3206, *supra*, seems contrary to the converse of that opinion, because it cuts off as an allowable deduction a loss where property is disposed of at a price greater than March 1, 1913 fair market value but less than original cost. The amendment to Article 1561 of Regulations 45 relative to the Revenue Act of 1918 is not based upon a construction of the statute but is based upon expediency in an attempt to retrieve from losers the taxes from which taxpayers realizing gains were relieved under the Goodrich *vs.* Edwards decision. These provisions of Article 1561 as amended were carried into the Revenue Act of 1921 in these words:

> "Sec. 202. (*a*) That the basis for ascertaining the gain derived or loss sustained from a sale

or other disposition of property, real, personal, or mixed, acquired after February 28, 1913, shall be the cost of such property; * * *

(*b*) The basis for ascertaining the gain derived or loss sustained from the sale or other disposition of property, real, personal, or mixed, acquired before March 1, 1913, shall be the same as that provided by sub-division (*a*); but—

(1) If its fair market price or value as of March 1, 1913, is in excess of such basis, the gain to be included in the gross income shall be the excess of the amount realized therefor over such fair market price or value;

(2) If its fair market price or value as of March 1, 1913, is lower than such basis, the deductible loss is the excess of the fair market price or value as of March 1, 1913, over the amount realized therefor; and

(3) If the amount realized therefor is more than such basis but not more than its fair market price or value as of March 1, 1913, or less than such basis but not less than such fair market price or value, no gain shall be included in and no loss deducted from the gross income. * * *"

When the Revenue Act of 1924 was enacted, the Revenue Act of 1921 had been effective for three years and the Treasury Department had had three years experience in its administration. The Revenue Act of 1924 makes important modifications in the provisions relating to the basis for determining gain or loss. It reenacts the rule adopted in Goodrich *vs.* Edwards, *supra,* relating to gains; but it rejects the rule for determining losses which was first announced in the Treasury Decision amending Article 1561, *supra,* and afterward carried into the Revenue Act of 1921, and in lieu thereof provides

that in the case of losses as well as in the case of gains, the basis shall be the March 1, 1913, value or the original cost, whichever is greater, where the property was acquired before March 1, 1913, in these words:

> "Sec. 204. (*b*) The basis for determining the gain or loss from the sale or other disposition of property acquired before March 1, 1913, shall be (A) the cost of such property * * *, or (B) the fair market value of such property as of March 1, 1913, whichever is greater. In determining the fair market value of stock in a corporation as of March 1, 1913, due regard shall be given to the fair market value of the assets of the corporation as of that date."

In the light of this experience, why should the Revenue Act of 1918 be construed to deny a deductible loss realized upon the sale of property during 1919 at a price below the March 1, 1913 value but above the original cost, contrary to the very plain and unambiguous language of the statute?

As stated, the basis for determining gains involves the determination of gross income. The rule established in Goodrich *vs.* Edwards, *supra,* has been adopted by Congress in the Revenue Acts of 1921 and 1924, either because of substantial justice or because of some question of constitutional doubt. In the case of losses, however, it has proved unjust or impracticable to limit the deduction for losses upon the sale of property acquired prior to March 1, 1913, to the original cost or the value on March 1, 1913, whichever is lower, and after three years experiment with this provision in the Revenue Act of 1921, Congress, upon the recommendation of the Treasury Department, in the Revenue Act of 1924 has definitely provided that the basis for determining losses sustained upon the sale of property

acquired prior to March 1, 1913, shall never be less than the March 1, 1913 value, nor less than the original cost if the original cost was in excess of such value.

If the plain language of the Revenue Act of 1918 is to be modified by construction, it is submitted that in view of the rule that a taxing statute is always to be construed most strongly against the Government, and in view of the experience of the Treasury Department under the Revenue Act of 1921, the rule for determining loss under the Revenue Act of 1924 would be a more just and appropriate construction than the rule for determining loss, as provided in the Revenue Act of 1921.

As stated in the beginning of this brief, however, the statutory language is so clear in the determination of deductions for losses, that no extraneous construction is required and the deductible loss should be based on the value on March 1, 1913, irrespective of the amount of original cost.

Respectfully submitted by

SANFORD ROBINSON,
Office and Post Office Address,
No. 26 Liberty Street,
New York, N. Y.
As *Amicus Curiæ*.

Dated: New York, N. Y., December 31, 1924.

FILED
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No. 527.

IN THE

Supreme Court of the United States,

OCTOBER TERM, 1924.

THE UNITED STATES,

Appellant,

v.

HARRIET ROGERS FLANNERY AND J. ROGERS FLANNERY,
EXECUTORS OF THE ESTATE OF JAMES J. FLANNERY, DECEASED,

Respondent.

BRIEF SUBMITTED WITH THE CONSENT OF THE COURT.

ARTHUR BALLANTINE,
BERNHARD KNOLLENBERG,
Amici Curiae.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1924

THE UNITED STATES, Appellant, v. HARRIET ROGERS FLANNERY and J. ROGERS FLANNERY, Executors of the Estate of James J. Flannery, Deceased, Respondent.	No. 527.

APPEAL FROM THE COURT OF CLAIMS

BRIEF SUBMITTED WITH THE CONSENT OF THE COURT BY ARTHUR A. BALLANTINE AND BERNHARD KNOLLENBERG, AMICI CURIAE.

Statement.

The issue in *Waialua Agricultural Company, Limited,* v. *The United States,* now pending in the United States Court of Claims, is the same as that in the present case and the two cases were

argued at the same time in the Court of Claims. The Government's demurrer to claimant's petition in the *Waialua* case was overruled on May 26, 1924, and proof of March 1, 1913, value is now being made in the Court of Claims. The issue in both cases is whether on the sale of property acquired before March 1, 1913, the proceeds are to be compared with the March 1, 1913 value or with the cost of the property as the underlying basis for computing the statutory gain or loss from the sale.

The Statute and Treasury Regulations.

The loss occurred in 1920 and its status for income tax purposes is governed by the provisions of the Revenue Act of 1918 (40 Stat. 1057 *et seq.*).

TITLE II.—INCOME TAX.

* * * * *

"Basis for determining Gain or Loss.

Sec. 202(*a*) That for the purpose of ascertaining the gain derived or loss sustained from the sale or other disposition of property, real, personal, or mixed, the basis shall be—

(1) In the case of property acquired before March 1, 1913, the fair market price or value of such property as of that date; and

(2) In the case of property acquired on or after that date, the cost thereof; or the in-

ventory value, if the inventory is made in accordance with section 203."

* * * * *

"Gross Income Defined.

Sec. 213. That for the purposes of this title (except as otherwise provided in section 233) the term 'gross income'—

(*a*) Includes gains, profits, and income derived from salaries, wages, or compensation for personal service (including in the case of the President of the United States, the judges of the Supreme and inferior courts of the United States, and all other officers and employees, whether elected or appointed, of the United States, Alaska, Hawaii, or any political subdivision thereof, or the District of Columbia, the compensation received as such) of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

* * * * *

Sec. 214. (*a*) That in computing net income there shall be allowed as deductions:

(4) Losses sustained during the taxable year and not compensated for by insurance or otherwise, if incurred in trade or business;

(5) Losses sustained during the taxable year and not compensated for by insurance or otherwise, if incurred in any transaction entered into for profit, though not connected with the trade or business; but in the case of a nonresident alien individual only as to such transactions within the United States;

(6) Losses sustained during the taxable year of property not connected with the trade or business (but in the case of a nonresident alien individual only property within the United States) if arising from fires, storms, shipwreck, or other casualty, or from theft, and if not compensated for by insurance or otherwise;

"Tax on Corporations.

Sec. 230. (*a*) That, in lieu of the taxes imposed by section 10 of the Revenue Act of 1916, as amended by the Revenue Act of 1917, and by section 4 of the Revenue Act of 1917, there shall be levied, collected, and paid for each taxable year upon the net income of every corporation a tax at the following rates:

(1) For the calendar year 1918, 12 per centum of the amount of the net income in excess of the credits provided in section 236; and

(2) For each calendar year thereafter, 10 per centum of such excess amount."

* * * * *

"Net Income Defined.

Sec. 232. That in the case of a corporation subject to the tax imposed by section 230 the term 'net income' means the gross income as defined in section 233 less the deductions allowed by section 234, * * *."

"Gross Income Defined.

Sec. 233. (*a*) That in the case of a corporation subject to the tax imposed by section 230 the term 'gross income' means the gross income as defined in section 213, * * *."

"Deductions Allowed.

Sec. 234. (*a*) That in computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions:

* * * * *

(4) Losses sustained during the taxable year and not compensated for by insurance or otherwise;"

* * * * *

Section 301 providing for war profits and excess profits taxes has no material bearing on the question at issue and is, therefore, not quoted in this brief.

The original, contemporaneous Treasury Regulations.

Treasury Regulations 45, construing the 1918 Act, provided, as originally issued, that:

"Art. 1561—Basis for determining gain or loss from sale.—For the purpose of ascer-

taining the gain or loss from the sale or exchange of property the basis is (*a*) its fair market price or value as of March 1, 1913, if acquired prior thereto, or (*b*), if acquired on or after that date, its cost or its approved inventory value. * * *."

This Regulation was in force from 1919 until July 28, 1921.

The Treasury Department's change of position.

On July 28, 1921, the Commissioner of Internal Revenue issued *Treasury Decision 3206,* which amended Article 1561 of Regulations 45 to read as follows:

"Art. 1561. Basis for determining gain or loss from sale.—For the purpose of ascertaining the gain or loss from the sale or exchange of property the basis is the cost of such property, or if acquired on or after March 1, 1913, its cost or its approved inventory value. But * * * in the case of property acquired before March 1, 1913, when its fair market value as of that date is lower than its cost, the deductible loss is the excess of such fair market value over the amount realized therefor."

This is the Regulation now in force.

ARGUMENT.

I.

The language and intent of the 1918 Act fix the March 1, 1913, value of the stock as the basis on which to determine the deductible loss.

A. The Act plainly states that the basis for computing gain or loss on the sale of property acquired before March 1, 1913, shall be the March 1, 1913, value of the property.

The Government's position is, in effect, (1) that the meaning of the word "losses" as used in the sections of the Act (Secs. 214 and 234) providing for the deduction of losses, is to be sought, not in the statute itself, but in the common meaning of the word, and (2) that, as commonly used, "loss" means the difference between selling price and cost. Sec. 202(*a*) relating to the determination of gain or loss on the sale of property was not, the Government maintains, intended to fix March 1, 1913 value as the basis for determining statutory gain or loss, but was intended simply to restrict for tax purposes gains and losses determined in the first instance on the basis of cost.

Appellee's position is that the meaning of the word "losses", as used in the 1918 Act, is defined in Sec. 202(*a*) of the Act, and that the common meaning of "losses", if different from the statu-

tory definition, must, of necessity, yield to the statutory definition. (*Pirie* v. *Chicago Title & Trust Co.*, 182 U. S. 438, 442 (1901)).

Sec. 202(*a*) of the 1918 Act provides:

> "That for the purpose of ascertaining the gain derived or loss sustained from the sale * * * of property, * * * the basis shall be—
>
> (1) In the case of property acquired before March 1, 1913, the fair market price or value of such property as of that date; and
>
> (2) In the case of property acquired on or after that date, the cost thereof; or the inventory value, if the inventory is made in accordance with section 203."

Sec. 202 is one of the preliminary, definition sections and was plainly intended to define the meaning of the words "gains" and "losses", in the later, substantive provisions of the Act. This is recognized, except in the present connection, by the Treasury Department, which holds, for example, that statutory gain and loss on the sale of inventoried property is, as defined in Sec. 202(*a*) (2), the difference between the selling price and the inventory value, and not the difference between the selling price and cost. Furthermore, the provisions in Sec. 202(*a*) (2) that "cost" shall be the basis for determining gain or loss on the sale of one class of property, namely, property acquired *on or after* March 1, 1913,

clearly shows that Sec. 202(*a*) was intended to define the words "gains" and "losses", since, if the purpose of the Section was to limit gains and losses, defined by an extrinsic standard in all cases on the basis of cost, the insertion of this provision designating cost as the basis in only one class of cases, would have been superfluous and misleading.

In defining "gains" and 'losses" in Sec. 202(*a*), Congress clearly prescribed and intended March 1, 1913, value, and not cost, as the basis for computing statutory gains and losses on the sale of property acquired before March 1, 1913. This is established by the clear and controlling language of the statute and by the circumstances under which it was enacted.

At the time the 1918 Act was adopted, the Treasury Department held that, under the *1916* Act, statutory gain or loss on the sale of property acquired before March 1, 1913, must be computed on the basis of the March 1, 1913, value of the property without reference to its cost. This position was set forth in Article 90 of Treasury Regulations 33, Revised as follows:

> "In cases where securities or other assets, real, personal, or mixed, acquired prior to March 1, 1913, are disposed of during the year, the gain or loss thereon will be based upon the difference between the price at which disposed of and the fair market price

> or value of such assets as of March 1, 1913, or the difference between the price at which disposed of and the *cost* if acquired subsequent to that date."

The above language was embodied, without any material change, other than the insertion of a provision as to inventory value, in Sec. 202(*a*) of the 1918 Act.

It is difficult to suggest how, in brief compass, Congress could have more clearly expressed its intention to embody, in the 1918 Act, the Treasury Department's construction of the 1916 Act. Sec. 202(*a*) of the 1918 Act says that March 1, 1913, value shall be *"the basis", i. e.*, according to Webster, the "foundation; base; groundwork" for determining gain or loss on the sale of property acquired before March 1, 1913. The word "basis" of itself clearly shows that March 1, 1913, value was intended as the underlying basis for computing gain or loss and not as a limitation (as contended by the Government) on gain or loss computed on some other basis. Moreover, it is undisputed that cost was intended as *the basis—i. e.*, the underlying foundation,—for determining gain or loss on the sale of property acquired on or after March 1, 1913. Since the word "basis" in Sec. 202(*a*) indisputably means *basis,* as applied to the sale of property acquired on or after March 1, 1913, how can it reasonably be maintained that it means something

wholly different as applied to the sale of property acquired before March 1, 1913?

The intention to prescribe March 1, 1913, as the basis in the case of property acquired before March 1, 1913, and cost only in the case of property acquired on or after March 1, 1913, is shown not only by the unambiguous language of Sec. 202(*a*), but by the other provisions of the 1918 Act similar to, and therefore having a material bearing on the interpretation of, Sec. 202(*a*). These provisions are Sec. 202(*b*) relating to the determination of taxable profit on the exchange of securities, and Secs. 214(*a*) (10) and 234(*a*) (9) relating to the allowance for depletion.

Sec. 202(*b*), dealing with the *exchange of securities*, provides that:

> "When in the case of * * * reorganization, merger or consolidation the aggregate par or face value of the new stock or securities received is in excess of the aggregate par or face value of the stock or securities exchanged, * * * the amount of the excess in par or face value shall be treated as a gain to the extent that the fair market value of the new stock or securities is greater than the cost (or if acquired prior to March 1, 1913, the fair market value as of that date) of the stock or securities exchanged."

Sec. 234(*a*)(9) relating to *depletion* in the case of corporations, provides:

> "That in computing the net income of a corporation * * * there shall be allowed as deductions: * * *
>
> (9) In the case of mines, * * * and timber, a reasonable allowance for depletion * * * based upon cost * * * *Provided,* That in the case of such properties acquired prior to March 1, 1913, the fair market value of the property (or the taxpayer's interest therein) on that date shall be taken *in lieu of cost up to that date.*" (Italics ours.)

Sec. 214(*a*)(10), relating to depletion in the case of individuals, contains precisely the same language as Sec. 234(*a*)(9).

These provisions, although varying slightly in wording and arrangement, all reflect the fundamental intention of Congress, in the 1918 Act, to substitute March 1, 1913 value for cost in matters relating to property acquired before March 1, 1913.

The language of the 1918 Act plainly provides that the statutory gain or loss on the sale of property acquired before March 1, 1913, shall be computed on the basis of the March 1, 1913, value of the property and not on the basis of cost.

B. Under decisions of the Supreme Court in force at the time the 1918 Act was adopted, the March 1, 1913, value of property owned by a taxpayer on that date constitutes the "capital value" of the property for income tax purposes, and loss determined on the basis of March 1, 1913 value is a real and not a "fictitious" loss.

The thought underlying the Government's contention that, despite the clear language to the contrary, Congress intended to provide in the 1918 Act that gain or loss on the sale of property acquired before March 1, 1913, shall be determined on the basis of cost, is set forth on pages 15, 16 and 22 of its brief in the *Waialua* case, argued in the Court of Claims along with the present case, as follows:

> "It is obvious that section 213 proposes to tax gains or profits derived from sales or dealings in property whether real or personal. It is likewise apparent that section 234 allows as a deduction losses sustained during the taxable year and not compensated for by insurance or otherwise.
>
> Congress clearly intended in the foregoing sections that gains and profits mean *actual* gains and profits and that the words 'losses sustained' mean *actual* losses. 'Paper' or fictitious gains or losses are not included, and are not intended to be included, as taxable or deductible, as the case may be."

* * * * *

> "* * * The date, March 1, 1913, was intended to be used *as a guide* in ascertaining *the amount* of gain derived or loss sustained, but original *cost* must *first* be taken into consideration, and if there is no actual gain on the entire transaction there is no taxable gain; and if there is no actual loss on the entire transaction there is no deductible loss." (Italics ours.)

It is not conceded that a loss, computed on the basis of the fair March 1, 1913 value of property owned on that date, is, as assumed by the Government, a "fictitious" loss. The test of the fictitiousness or artificialty of a loss is not whether it is based on cost or on some value other than cost, but whether there is some reasonable ground for the selection of the basis designated.

That a loss is no less "actual" because based upon fair market value as of a given date rather than upon cost, is clearly recognized in the case of property received by inheritance. If such property is sold by the heir at less than its value at the time of the inheritance, no one would question that the difference between the value of the property at the time of the inheritance and the selling price is an actual loss, although the cost of the property to the seller who sustained the loss, was nothing. The Treasury Department, even without specific authorization in the statute, has consistently held that the deductible loss on the sale

of property by the heir is the difference between the selling price and the value at the time of inheritance. (Article 1562 of Regulations 45; Art. 1563 of Reg. 62).

This principle is given effect in the provisions of the 1918 Act with respect to inventories. If a dealer in securities inventories securities at $12,000 which cost him $10,000, and during the next year sells these securities for $8,000, his deductible loss, under Sec. 202(*a*) of the 1918 Act, is $4,000, not $2,000. The Treasury Regulations give effect to this provision. (Article 1561 of Regulations 45.) The reason that the loss in this case is readily perceived to be an actual, not a fictitious loss, is the obvious appropriateness of taking the last inventory value, in place of cost, as the basis for computing the loss. The same is true as to March 1, 1913, value in relation to the determination of loss for income tax purposes. The Courts have consistently held that increase in value which accrued prior to March 1, 1913, the date when the Sixteenth Amendment became effective, must be regarded for income tax purposes as "capital value". Consequently, March 1, 1913, value is the most appropriate basis that could have been adopted for computing the deductible loss on the sale of property acquired before March 1, 1913, and the loss computed on this basis is not an artificial or fictitious loss.

This question as to the alleged "fictitiousness" of a loss based on March 1, 1913, value has been discussed at some length solely because of the Government's great emphasis on this point. The question has, at most, but a remote bearing on the construction of the statute, because, even if a loss exceeding the difference between selling price and cost were a "fictitious" loss, it clearly would not be within the province of the Court to substitute a loss, if any, determined on the basis of cost, for the loss as defined by the Act. Nothing is better settled than that where, as in the present case, the language of the Act is unambiguous and no constitutional difficulties are involved, this Court will not impute to Congress an intention other than that expressed in the language of the statute.

In *United States* v. *Standard Brewery,* 251 U. S. 210, 217, Mr. Justice Day, speaking for the unanimous Court, said:

> "Nothing is better settled than that in the construction of a law its meaning must first be sought in the language employed. If that be plain, it is the duty of the courts to enforce the law as written, provided it be within the constitutional authority of the legislative body which passed it. *Lake County* v. *Rollins,* 130 U. S. 662, 670, 671; *Bate Refrigerating Co.* v. *Sulzberger,* 157 U. S. 1, 33;

United States v. *Bank*, 234 U. S. 245, 258; *Caminetti* v. *United States*, 242 U. S. 470, 485."

This rule applies with peculiar force when, as in the present case, the provisions of the Act are not only clear, but, in the light of the circumstances prevailing at the time the statute was enacted, could not have been more reasonable and appropriate.

On May 20, 1918, a few months before the 1918 Act was drafted, the Supreme Court rendered its opinion in the case of *Doyle* v. *Mitchell Brothers Company*, 247 U. S. 179, which arose under the Corporation Excise (Income) Tax Law of 1909. The case involved the question of whether the taxable income on sales in the years 1909 to 1912 of the Company's timber lands acquired before January 1, 1909, should be computed on the basis of the *cost* of the timber lands or on the basis of their *value on January 1, 1909*,—the date as of which the Corporation Income Tax Law of 1909 took effect. Although the 1909 Act made no reference whatsoever to January 1, 1909, value, the Court nevertheless held that "income", as used in the Act, from the sale of property acquired before January 1, 1909, was the difference between selling price and January 1, 1909, value, rather than the difference between selling price and cost.

The Court's decision was based on the following reasoning:

> "In order to determine whether there has been gain or loss, and the amount of the gain, if any, we must withdraw from the gross proceeds an amount sufficient to restore the *capital value* that existed at the commencement of the period under consideration. * * *
>
> When the act took effect, plaintiff's timber lands, with whatever value they then possessed, were a part of its capital assets, and subsequent change of form by conversion into money did not change the essence. * * *
>
> It may be observed that it is a mere question of methods, not affecting the result, whether the amount necessary to be withdrawn *in order to preserve capital intact* should be deducted from gross receipts in the process of ascertaining gross income, or should be deducted from gross income in the form of a depreciation account in the process of determining net income. *In either case the object is to distinguish capital previously existing from income taxable under the act*". (pp. 185, 187, 188). (Italics ours.)

Two weeks later, on June 3, 1918, the Supreme Court affirmed the decision of the Circuit Court of Appeals in *Lynch* v. *Turrish*. In this case the Circuit Court of Appeals for the Eighth Circuit had held that no taxable income resulted from the receipt by Turrish of a liquidating dividend which

exceeded the cost but did not exceed the March 1, 1913, value of his stock in the liquidating corporation, on the ground that:

> "All * * * *the value of the stock of the plaintiff,* whether it was due to capital assets, or income, or gains, or profits, or all of these combined, *had arisen and accrued and had become their property before March 1, 1913.*" (p. 657). (Italics ours.)
>
> *Lynch, Collector* v. *Turrish,* 236 Fed. 653 (aff. 247 U. S. 221).

The Treasury Regulations issued under the 1916 Act already provided that gain or loss on the sale of property acquired before March 1, 1913, should be determined on the basis of March 1, 1913, value (*supra,* pp. 9-10; also Article 4, 101, 109, 111, 112, 116, 118, 119, 147, 157, 167 and 168 of Regulations 33, revised). As a result of the *Mitchell Bros. Co.* and *Turrish* decisions, this ruling was extended to the two previous income tax statutes—the 1909 and 1913 Acts—as well. *Treasury Decision 2740,* issued June 24, 1918.

It therefore clearly appeared, at the time the 1918 Act was adopted, that March 1, 1913 value was the most appropriate basis that could be designated for determining the statutory gain or loss on the sale of property acquired before March 1, 1913.

The explicit provision of Sec. 202(*a*) that in determining the gain or loss from the sale of property acquired before March 1, 1913, the basis shall be the value of the property as of that date, the immediate context of this provision, the other material sections of the Act, and the circumstances at the time the Act was adopted, all unite to show beyond the possibility of doubt that Congress intended, as it so plainly said, that under the 1918 Act the basis for determining gain or loss on the sale of property acquired before March 1, 1913, shall be the March 1, 1913, value of the property.

II.

The decisions in the Goodrich and Brewster cases construing the 1916 Act do not sustain the Government's contention that cost was the intended basis under the 1918 Act, since the provisions of the 1918 Act relating to the determination of gain or loss from the sale of property are vitally different from the corresponding provisions of the 1916 Act.

In the *Goodrich* and *Brewster* cases (255 U. S. 527 and 536 (May 28, 1921)), this Court held that in the 1916 Act the word "gains" as applied to the sale of property, irrespective of whether the property was acquired before or after March 1, 1913, meant the difference between sell-

ing price and cost. As shown hereinafter (*infra,* pp. 28-31) it does not follow that the Court would also have held, had the issue been presented, that the word "losses" as used in the 1916 Act meant the difference between selling price and cost. But even if the decisions in the *Goodrich* and *Brewster* cases implied that losses as well as gains must, under the 1916 Act, be computed on the basis of cost, the Government's contention that the words "gains" and "losses" must be given the same meaning in the 1918 Act, is unsound.

The Government appears to assume that the *Goodrich* and *Brewster* decisions hold or imply that the word "gain" shall be construed in income tax laws generally, including the 1918 Act, in the fixed sense of economic gain. Starting with this preconceived theory of the meaning of "gain", the Government disregards the vital differences in the language of the 1916 and 1918 Acts and the highly significant circumstances under which the 1918 Act was adopted (*supra,* pp. 17-19) and reads the 1918 Act not as it is, but as it presumably would have been, had Congress intended the gain and loss provisions in the 1918 Act to have the same meaning as those in the 1916 Act.

But the *Goodrich* and *Brewster* decisions do not sustain this theory. All that the Court was called upon to do and did do in the *Goodrich* and *Brewster* cases was to address itself to the meaning of

the word "gain" as used *in the 1916 Act.* The Court did not hold or imply that where, as in the 1918 Act, the language of the statute, and the circumstances under which the statute was enacted, clearly show that a different meaning was intended, it would not freely give effect to the expressed intention of Congress.

As pointed out by Mr. Justice Holmes, in *Towne* v. *Eisner:*

> "A word is not a crystal, transparent and unchanged, it is the skin of a living thought and may vary greatly in color and content according to the circumstances and the time in which it is used" (245 U. S. 418, 425 (1918)).

The language of the 1916 Act, construed in the *Goodrich* and *Brewster* cases, reads as follows:

> "Sec. 2(*a*) That, subject only to such exemptions and deductions as are hereinafter allowed, the net income of a taxable person shall include gains, * * * from * * * sales, or dealings in property, * * *.
>
> * * * * *
>
> (*c*) For the purpose of ascertaining the gain derived from the sale or other disposition of property, real, personal, or mixed, acquired before March first, nineteen hundred and thirteen, the fair market price or value of such property as of March first,

> nineteen hundred and thirteen, shall be the basis for determining the amount of such gain derived."

It will be observed that the first clause of subsection (*c*) is merely introductory and that the words "the fair market price or value of such property as of March first, nineteen hundred and thirteen" are the subject of the phrase "shall be the basis for determining the *amount* of such gain". March 1, 1913 value is here designated not as the underlying basis for determining whether the transaction resulted in a statutory "gain" or in a statutory "loss", but merely as the basis for determining "the amount" of taxable gain, thus implying that some other basis shall be used, in the first instance, in determining whether the transaction resulted in statutory gain or statutory loss.

This limited function of the provisions as to March 1, 1913 value in the 1916 Act is brought out even more clearly in the language of the section of the 1916 Act dealing with losses deductible by non-resident aliens:

> "Sec. 6. That in computing net income * * * there shall be allowed as deductions * * *
>
> Fourth. Losses actually sustained during the year, * * * Provided, That for the purpose of ascertaining *the amount* of such loss or losses * * * from * * *

> any kind of property acquired before March first, nineteen hundred and thirteen, the fair market price or value of such property as of March first, nineteen hundred and thirteen, shall be the basis for determining *the amount of such loss or losses* sustained." (Italics ours.)

In sharp contrast to the 1916 Act, the 1918 Act provides that March 1, 1913 value shall be the basis for *"ascertaining the gain derived or loss sustained"*. This, taken in conjunction with other significant changes, plainly negatives the implication of the 1916 Act that whether a statutory gain or loss has been realized shall first be determined on some basis other than March 1, 1913 value. It shows that, in the 1918 Act, March 1, 1913 value was intended as the basis for determining whether, for purposes of the Act, the transaction resulted in a gain, in a loss, or in an even break, as well as for determining the *amount* of the statutory gain or loss, if any.

A second significant difference in the two Acts is the ***difference in location*** of the provision as to March 1, 1913 value, in the respective Acts. The natural place to insert a limitation upon the amount of "gain" or "loss" which,—but for such limitation,—would be taxable or deductible, is, of course, immediately after the respective provisions for the taxation or deduction of such "gain" or "loss". In the provisions of the 1916 Act dealing

with the taxable gain of individuals—the provisions construed in the *Goodrich* and *Brewster* cases—the reference to March 1, 1913 value is found in precisely this juxtaposition, *i. e.,* it is in the same section *with* and *after* the provision for the taxation of "gains".

In the 1918 Act, however, as previously pointed out, the provisions as to the determination of gain or loss on the sale of property, including the provision as to March 1, 1913 value, appear in a section *wholly apart* from and *preceding* the sections providing for the taxation of "gains" and the deduction of "losses". Moreover, these provisions are found precisely where provisions intended to define the statutory meaning of "gains" and "losses" would naturally be inserted, namely, among the preliminary sections (Secs. 1 and 200 to 206 of the Act), devoted largely to defining and explaining the meaning of words and phrases used in subsequent portions of the Act. The incongruity of inserting a provision intended (according to the Government's contention) not as a definition but as a *limitation,* before the provision which it was intended to restrict, is evidently recognized by the Government. In setting forth the 1918 Act, the Government (pp. 2-3 of its Brief in this case) has interpolated Sec. 202(*a*) *immediately after* the provision in Sec. 214 for the deduction of losses.

A third material difference between the 1916 Act and the 1918 Act is the insertion in the later Act of a paragraph providing for "cost" as the basis for determining gain or loss on the sale of property acquired *on or after March 1, 1913*. The absence of any such provision in the 1916 Act enabled this Court to hold, without any inconsistency with the language of the statute, that, under that Act, cost was intended as the basis in all cases. The insertion, in the 1918 Act, of the provision that, in the case of a single designated class of property, gain and loss shall be determined on the basis of *cost*, clearly indicates that, under this Act, gain and loss on the sale of other property—including all property acquired before March 1, 1913, and inventoried property acquired on or after March 1, 1913—is to be determined on some different basis or bases.

A fourth difference between the two Acts is that the 1916 Act provides for the deduction of "losses *actually* sustained", whereas in the 1918 Act the word "actually" is dropped. If, as contended by the Government, *"actual"* losses are limited to losses measured by the difference between selling price and cost, the dropping of the word "actually" is of great significance as indicating that under the 1918 Act Congress did not intend to restrict deductible losses to losses measured by the difference between selling price and cost.

These various changes plainly show that Congress intended, in the 1918 Act, to amend the provisions of the 1916 Act relative to the determination of statutory gains and losses in order to bring these provisions into clear conformity with the Treasury Department's interpretation of the 1916 Act. It is a well-recognized principle of construction that where Congress re-enacts, in a later statute, the provisions of an earlier Act having an established administrative interpretation, it is to be presumed that Congress intended, in the later statute, to use the language of the earlier Act in the sense in which it was being interpreted under the earlier Act.

National Lead Company v. *United States,* 252 U. S. 140, 146-7 (1920);
Copper Queen Mining Company v. *Arizona Board,* 206 U. S. 474, 479 (1907);
United States v. *Falk,* 204 U. S. 143, 152 (1907).

The logic of this rule, of course, applies with extraordinary force in a case, like the present, where Congress has, in the later Act, *amended the language of the earlier Act to conform* to the construction placed upon the earlier Act by the Executive.

The Government's contention that the *Goodrich* and *Brewster* decisions are controlling in the pres-

ent case is based on the assumption that the provisions of the 1918 Act with respect to the determination of statutory gain and loss are substantially the same as those of the 1916 Act, whereas, both as to language and location, the provisions of the 1918 Act are vitally different from those of the 1916 Act and unmistakably show that in the later Act Congress intended and prescribed March 1, 1913 value as the basis for determining gain or loss on the sale of property acquired before March 1, 1913.

III.

Any doubt as to the constitutionality of including in taxable income an amount in excess of the gain computed on the basis of cost does not apply to the allowance of a deductible loss in excess of the loss computed on the basis of cost.

As the basis for the discussion under the preceding heading, it was assumed that, as contended by the Government, the Court would construe the provisions of the 1916 Act as to deductible loss in the same way that the provisions as to taxable gain were construed in the *Brewster* and *Goodrich* cases. But the validity of this assumption is not admitted, since constitutional considerations which must have influenced the de-

cision as to *gains*, do not apply to the construction of the provisions as to *losses*.

In the appellant's brief in the *Goodrich* case, (p. 63 of the brief), the constitutional question with respect to the taxation of gain was set forth as follows:

> "It is submitted that it is reasonably manifest that a construction of the Income Tax Law of 1916 which would practically result in levying a tax upon and measured by what is essentially diminished or reduced capital would be unconstitutional as being in substance and effect a direct tax payable solely in respect of capital or out of the proceeds of capital. At any rate, there are certainly 'grave doubts upon that score.' In such a case the rule in this court is to avoid a conclusion which might render a statute even of doubtful constitutionality (*United States* v. *Standard Brewery*, 251 U. S. 210, 220; *United States* v. *Jin Fuey Moy*, 241 U. S. 394, 401; *United States* v. *Delaware & Hudson Co.*, 213 U. S. 366), and to adopt a construction which will avoid such doubts, if reasonably permissible. Moreover, equally well-settled is the rule that any doubt as to the intent of a tax law will be resolved in favor of the taxpayer. *Gould* v. *Gould*, 245 U. S. 151; *Eidman* v. *Martinez*, 184 U. S. 578, 583-590."

The Solicitor General, not only made no reply to this argument, but (abandoning the Treasury Department's construction of the 1916 Act, which

the Government had maintained in the lower court), expressly conceded in his brief in the *Goodrich* case that

> "If this construction" [that March 1, 1913, value, in place of cost, was intended as the basis for determining taxable gain on the sale of property acquired before March 1, 1913] "of the law is correct, a *serious constitutional question arises.* * * * The contention is that, *under the commissioner's construction* of the law, *something is taxed which is not,* in fact, *income and which Congress was therefore without the power to tax* except by apportionment." (Italics ours.)

Since it is an established rule of construction that a statute will be construed, if reasonably possible, to avoid questions of possible unconstitutionality, (*United States* v. *Delaware & Hudson Company,* 213 U. S. 366, 407-8 (1909)), the decision in the *Goodrich* case was doubtless influenced by the Solicitor General's concession on the constitutional point. The decision might well, therefore, have been different had the issue been one as to losses, as to which no constitutional question exists.

That Congress may allow such deductions as it sees fit, in defining net taxable income, (subject, of course, to the ordinary constitutional restrictions as to uniformity, etc.), has been accepted as settled ever since the decision in *Brushaber* v. *Union Pacific Railway Company,* 240 U. S. 1

(1916), in which the Supreme Court summarily dismissed the contention that the 1913 Act was unconstitutional because providing for certain non-economic exemptions and deductions. There has never been any question, for example, of the validity of the provisions of the 1918 Act permitting deductions for "losses" by fire or other casualty of property held for personal use, "taxes" on residential or other property from which no income is derived or expected, "interest" on non-business indebtedness, and depletion based on March 1, 1913 value in excess of cost. *A fortiori* the allowance of a deductible loss based on March 1, 1913 value, such value having been held to be "capital value" for income tax purposes, is open to no possible question, (*the Mitchell Bros. Co.* and *Turrish* decisions, pp. 17-19, *supra*).

Constitutional necessity, if any, of permitting taxpayers to use cost, if more than March 1, 1913 value, as the basis for computing taxable gain, would not sustain the denial to taxpayers of a right, conferred by statute, of using March 1, 1913 value, in place of cost, as the basis for computing losses. As said by this Court in *Supervisors* v. *Stanley*, 105 U. S. 305, 312 (1881):

> "in a statute which contains invalid or unconstitutional provisions, that which is unaffected by these provisions, or which can stand without them, must remain. If the valid and invalid are capable of separation, only the latter are to be disregarded;"

IV.

The provisions of the 1921 and 1924 Acts relative to the determination of statutory gain and loss furnish additional evidence that, in the 1918 Act, March 1, 1913 value, in lieu of cost, was the prescribed and intended basis for determining gain or loss on the sale of property acquired before March 1, 1913.

The 1921 Act:

In the 1921 Act Congress provided that whether a statutory gain or loss had been realized should be determined in the first instance on the basis of cost. March 1, 1913, value was only to be referred to as a means of determining what part of the gain or loss determined on the basis of cost should be included in computing net taxable income. The Government contends this same method was provided for in the 1918 Act. Nothing, however, could more clearly show the unsoundness of this position than a comparative reading of the corresponding provisions of the two Acts set forth, in parallel columns, below.

1918 Act.	*1921 Act.*
"Sec. 202.(*a*) That for the purpose of ascertaining the gain derived or loss sustained from the sale or other disposition of property, real, personal or mixed, *the basis shall be*—	"Sec. 202.(*a*) That the basis for ascertaining the gain derived or loss sustained from a sale or other disposition of property, real, personal, or mixed, acquired after February 28, 1913,

1918 Act.

(1) *In the case of property acquired before March 1, 1913, the fair market price or value of such property as of that date;* and

(2) In the case of property acquired on or after that date, the *cost* thereof; or the inventory value, if the inventory is made in accordance with section 203. (Italics ours.)

1921 Act.

shall be the cost of such property; except that—

(1) In the case of such property, which should be included in the inventory, the basis shall be the last inventory value thereof;

* * * * *

(*b*) *The basis* for ascertaining the gain derived or loss sustained from the sale or other disposition of property, real, personal, or mixed, acquired *before* March 1, 1913, *shall be the same as that provided by subdivision* (*a*) [*i. e. "cost"*]; but—

(1) If its fair market price or value as of March 1, 1913, is in excess of such basis, the gain to be included in the gross income shall be the excess of the amount realized therefor over such fair market price or value;

(2) If its fair market price or value as of March 1, 1913, is lower than such basis, the deductible loss is the excess of the fair market price or value as of March 1, 1913, over the amount realized therefor; and

(3) If the amount realized therefor is more than such basis but not more than its fair market price or value as of March 1, 1913, or less than such basis but not less than such fair market price or value, no gain shall be included in and no loss deducted from the gross income." (Italics ours.)

The 1918 Act provides: (1) that the basis for ascertaining the gain or loss on the sale of property acquired before March 1, 1913, shall be the fair market value of such property as of that date; and (2) that the basis for determining the gain or loss on the sale of property acquired on or after March 1, 1913, shall be cost. The 1921 Act, on the contrary, specifically provides that *in both cases* the basis shall be *"cost"*.

This striking difference in language results from and expresses a difference in the conception of the function of March 1, 1913, value in the two Acts. When the 1918 Act was adopted, the approved basis for determining gain or loss on the sale of property acquired before March 1, 1913, was the March 1, 1913 value of the property. (*supra*, pp. 17-19). The Supreme Court in the *Mitchell Bros. Co.* and *Turrish* decisions had approved of this basis in principle and the Treasury Department consistently applied this basis under the 1916 Act.

At the time the 1921 Act was passed, the circumstances had vitally changed. The Solicitor General, in the *Brewster* case, had repudiated the Treasury Department's construction of the 1916 Act, partly on the ground that it raised "a serious constitutional question", and this Court, shortly before the 1921 Act was drafted, held in the *Brewster* case that the intended basis under the 1916 Act was cost. (pp. 20, 30, *supra*). It

was doubtless this change in circumstances that led Congress to amend the provisions of the 1918 Act and to adopt, in the 1921 Act, the basis of cost rather than that of March 1, 1913, value.

If the amendments in the 1921 Act had been intended as a legislative interpretation of the 1918 Act Congress would unquestionably have said so, as it did in Section 1331 of the 1921 Act dealing with consolidated returns, which provides that:

> "The provisions of this Section are declaratory of the provisions of Title II of the Revenue Act of 1917."

The plain inference is that the striking and discriminating changes in the 1921 Act were made for the purpose of establishing a different basis under the 1921 Act than the one provided for in the 1918 Act.

> *Harriman* v. *Interstate Commerce Commission,* 211 U. S. 407, 422 (1908); *United States* v. *Field,* 255 U. S. 257, 265 (1921).

That Congress did not regard the basis of March 1, 1913 value as intrinsically inappropriate, is clearly shown by the fact that, even in the 1921 Act, Congress designated March 1, 1913 value as the basis on which to compute the statutory deductions for depletion, depreciation and loss by fire or other casualty, of property acquired before March 1, 1913. (Sec. 214(*a*) of the 1921 Act).

Analysis of the 1921 Act sustains and reenforces the position that, in the 1918 Act, Congress prescribed and intended March 1, 1913 value as the basis for determining statutory gain or loss on the sale of property acquired before March 1, 1913.

The 1924 Act:

The provisions of the 1924 Act with respect to the determination of gain or loss on the sale of property are as follows:

> Sec. 204(*a*): "The basis for determining the gain or loss from the sale or other disposition of property acquired after February 28, 1913, shall be the cost of such property; except that—
>
> (1) If the property should have been included in the last inventory, the basis shall be the last inventory value thereof;
>
> * * * * *
>
> (*b*) The basis for determining the gain or loss from the sale or other disposition of property acquired before March 1, 1913, shall be (A) the cost of such property * * * or (B) the fair market value of such property as of March 1, 1913, whichever is greater."
>
> Sec. 214(*a*) "In computing net income there shall be allowed as deductions; * * *
>
> (4) Losses sustained during the taxable year * * *;"

The provisions of the 1924 Act show that it is necessary, in computing taxable gain or deductible loss under that Act, to look to the language of the statute and not to what may be deemed to be the familiar meaning of the words "gains" and "losses". If the Government's contention in the present case were followed, the word "losses", as used in Sec. 214(*a*), would be held to mean the difference between selling price and cost, while the provisions of Sec. 204(*b*) as to March 1, 1913 value would be treated as a mere limitation on the loss, if any, based on cost. The provisions of Sec. 204(*b*) giving to the taxpayer the option of using March 1, 1913 value or cost whichever is greater, would thus be nullified. In construing the 1924 Act, the Treasury Department rejects any such unwarranted distortion of the Act. The Department recognizes that the meaning of the word "losses", as used in Sec. 214, is not to be sought in some extrinsic guide, but is to be accepted and applied as defined in the Act. (Article 1591 of the 1924 Regulations (Regulations 65)).

The language of the 1918 Act shows with equal clearness that the provisions of Sec. 202(*a*) of that Act were intended to define the meaning of the word "losses" as used in that Act.

V.

The respondent's construction of the 1918 Act is sustained by the decisions of the United States Circuit Court of Appeals and of the Court of Claims.

The question at issue in the present case has been passed upon in several decisions.

In *Ludington* v. *McCaughn,* the Circuit Court of Appeals for the Third Circuit, in a clear and comprehensive opinion written by Judge Woolley, sustained the deduction under the 1918 Act of a loss, based on March 1, 1913 value, which exceeded the loss computed on the basis of cost. (Corporation Trust Company 1924 Income Tax Service, p. 892; October 1, 1924.) This decision reversed the judgment of the United States District Court for the Western District of Pennsylvania in the *Ludington* case (290 Fed. 604 (1923)).

The only decision, other than that of the District Court in the *Ludington* case, holding that the deductible loss is limited to the difference between selling price and cost, is a decision, without opinion, by the New York Supreme Court, Appellate Division, Third Department, in *Bush* v. *Law,* 201 N. Y. Supp. 513 (1923), construing Sec.

353 of the New York Income Tax Law of 1919, which is substantially the same as Sec. 202(*a*) of the Federal Revenue Act of 1918. A strong dissenting opinion was written in the *Bush* case by Judge Hasbrouck.

In *Vance* v. *McLaughlin,* the United States District Court for the District of California held that March 1, 1913 value is the statutory basis, under the 1918 Act, for computing the deductible loss on the sale of property acquired before March 1, 1913, (Corporation Trust Company 1924 Income Tax Service, p. 829).

The Court of Claims, in its opinion in the present case, favorable to the claimant, fully considered and met the arguments relied on by the Government in this appeal. The Court said in part:

> "Section 214, under the heading 'Deductions allowed', provides that in computing net income there shall be allowed 'as deductions' a number of items listed as * * * (4) Losses sustained during the taxable year * * *.
>
> "The Act anticipated the question as to what are 'losses' that are thus authorized to be deducted because" (in Sec. 202(*a*)) "it prescribes a 'basis for determining gain or loss,' * * *.
>
> "It is a primary and general rule of statutory construction that the intent of the law-

maker is to be found in the language that he has used. * * *

"The present case has to do with losses sustained, and the loss which Congress authorized to be deducted was a loss measured by the difference between the price stated at one time and another time. Manifestly the meaning of losses sustained as the words appear in section 214 is not to be determined independently of other parts of the Act. * * * Congress could have omitted the basis for determining loss, but it did not do that, and inserted section 202 instead. Congress * * * carefully distinguished between 'property acquired before March 1, 1913' and property acquired on or after that date. As to the former, the price or value as of March 1, 1913, governs, and as to the latter, 'the cost thereof' governs. The first of these distinctions is wiped out if the cost prior to March 1 be required, and the second clause is useless if the original cost of the property must in every case be used in ascertaining the deductible loss."

This decision was followed by the Court of Claims in the *Waialua* case (Corporation Trust Company 1924, Income Tax Service, p. 837 (May 26, 1924)).

Conclusion.

For the reasons set forth in this brief and in the decision of the Court below, it is clear that the March 1, 1913 value was the prescribed and intended basis, under the 1918 Act, for determining the deductible loss on the sale of property acquired before March 1, 1913, and that the judgment of the Court below should be affirmed.

Respectfully submitted,

ARTHUR A. BALLANTINE,
BERNHARD KNOLLENBERG,
Amici Curiæ.

THE UNITED STATES *v.* FLANNERY ET AL., EXECUTORS OF THE ESTATE OF JAMES J. FLANNERY, DECEASED.

APPEAL FROM THE COURT OF CLAIMS.

No. 527. Argued January 12, 1925.—Decided April 13, 1925.

1. The Revenue Act of 1918 provided that net income should include "gains" derived from sales or dealings in property, §§ 212 (a), and 213 (a); that there should be allowed as deductions "losses" sustained during the taxable year "incurred in any transaction entered into for profit," § 214 (a); and that "for the purpose of ascertaining the gain derived or loss sustained from the sale or other disposition of property . . . the basis shall be—(1) In the case of property acquired before March 1, 1913, the fair market price or value of such property as of that date; and (2) In the case of property acquired on or after that date, the cost thereof." § 202 (a). *Held:*

(*a*) That the provisions of the act in reference to the gains derived and the losses sustained from the sale of property acquired before March 1, 1913, were correlative, and that whatever effect was intended to be given to the market value of property on that date in determining taxable gains, a corresponding effect was intended to be given to such market value in determining deductible losses;

(*b*) That the Act of 1918 imposed a tax and allowed a deduction to the extent only that an actual gain was derived or an actual loss sustained from the investment, and the provision in reference to the market value on March 1, 1913, was applicable only where there was such an actual gain or loss, that is, that this provision was merely a limitation upon the amount of the actual gain or loss that would otherwise have been taxable or deductible. *Goodrich* v. *Edwards*, 255 U. S. 527; *Walsh* v. *Brewster*, *Id.* 536. P. 100.

2. Decisions of this Court affecting the business interests of the country should not be disturbed except upon the most cogent reasons. P. 105.

59 Ct. Cls. 719, reversed.

APPEAL from a judgment of the Court of Claims allowing recovery of an income tax paid under protest.

The Solicitor General, with whom *Messrs. Nelson T. Hartson,* Solicitor of Internal Revenue, and *Frederick W. Dewart,* Special Attorney, were on the brief, for the United States.

Mr. Edward S. Burling, with whom *Mr. Spencer Gordon* was on the brief, for appellees.

Messrs. Richard W. Hale and *Reginald H. Smith* filed a brief as *amici curiae,* by special leave of Court.

Messrs. Sanford Robinson, Arthur Ballantine and *Bernhard Knollenberg,* also filed a brief as *amici curiae,* by special leave of Court.

MR. JUSTICE SANFORD delivered the opinion of the Court.

James J. Flannery bought, prior to March 1, 1913, certain corporate stock for less than $95,175. Its market value on March 1, 1913 was $116,325. He sold it in 1919 for $95,175, that is, for more than cost. He died in March, 1920. The executors of his estate in returning his income for the year 1919 deducted, as a loss, the difference between the market value of the stock on March 1, 1913, and the price received. The Commissioner of Internal Revenue disallowed the loss claimed, and an additional tax was assessed. The executors paid this under protest, and thereafter, a claim for refund having been denied, brought this action in the Court of Claims to recover the amount paid. Judgment was rendered in their favor. 59 Ct. Cls. 719.

The question presented is whether, under the income tax provisions of the Revenue Act of 1918,[1] a deductible loss was sustained by the sale of the stock in 1919 for more than it had cost, by reason of the fact that on March 1,

[1] Act of Feb. 24, 1919, c. 18, Title II, 40 Stat. 1057.

1913, between the dates of purchase and sale, it had a market value greater than the sale price.

This Act provided that net income should include "gains" derived from sales or dealings in property, §§ 212 (a), 213 (a); that there should be allowed as deductions "losses" sustained during the taxable year "incurred in any transaction entered into for profit", § 214 (a); and that "for the purpose of ascertaining the gain derived or loss sustained from the sale or other disposition of property . . . the basis shall be—(1) In the case of property acquired before March 1, 1913, the fair market price or value of such property as of that date; and (2) In the case of property acquired on or after that date, the cost thereof . . ." § 202 (a).

The United States contends that under § 214 (a) there was no deductible loss whatever unless the taxpayer had sustained an actual "loss" in the entire transaction by selling the property for less than it had cost; and that the effect of § 202 (a) was merely that if such an actual loss had been sustained in selling property acquired before March 1, 1913, only so much thereof could be deducted as was sustained after the latter date, that is, the difference between the market value on that date and the sale price.

The executors contend, on the other hand, that § 202 (a) established the market value of such property on March 1, 1913, as the sole basis for ascertaining the loss sustained, without regard to its actual cost; and that if such market value was higher than the sale price, this conclusively determined that there had been a deductible "loss" in the transaction, and fixed the amount thereof at the difference between the market value on that date and the sale price.

It is clear, in the first place, that the provisions of the Act in reference to the gains derived and the losses sustained from the sale of property acquired before March 1, 1913, were correlative, and that whatever effect was intended to be given to the market value of property on

that date in determining taxable gains, a corresponding effect was intended to be given to such market value in determining deductible losses. This conclusion is unavoidable under the specific language of § 202 (a) establishing one and the same basis for ascertaining both gains and losses.

Taking this as a premise, we think that the question of determining taxable gains is concluded, in accordance with the contention of the Government, by the decisions of this Court in *Goodrich* v. *Edwards*, 255 U. S. 527, and *Walsh* v. *Brewster*, 255 U. S. 536. These cases, which were decided in 1921, arose under the income tax provisions of the Revenue Act of 1916.[2] That Act provided, as did the Act of 1918, that the "gains" derived from sales or dealings in property should be included in net income[3], and also that the losses actually sustained in transactions entered into for profit should be allowed as deductions.[4] In the Act of 1916, however, the provisions for the ascertainment of the gains derived and losses sustained from the sale of property were not contained, as in the Act of 1918, in one provision, but in separate clauses of the same tenor and effect as the combined provision in the Act of 1918. Section 2 (c) provided that: "For the purpose of ascertaining the gain derived from the sale or other disposition of property . . . acquired before" March 1, 1913, "the fair market price or value of such property as of" March 1, 1913, "shall be the basis for determining the amount of such gain derived." The correlative clause relating to the ascertainment of loss was in precisely the same language except that the words "the loss" and "loss sustained" were used instead of the words "the gain" and "gain derived."[5]

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[2] Act of Sept. 8, 1916, c. 463, 39 Stat. 756.

[3] § 2 (a).

[4] § 5 (a) Fifth.

[5] § 5 (a) 4th.

In *Goodrich* v. *Edwards, supra,* in the second transaction involved, the taxpayer had acquired in 1912 certain corporate stock of the then value of $291,600. Its market value on March 1, 1913, was only $148,635.50. He sold it in 1916 for $269,346.25, being $22,253.75 less than its value when acquired, but $120,710.75 more than its value on March 1, 1913. A tax was assessed on the latter amount, which was sustained by the trial court. The Government confessed error in this judgment. After reciting this fact and setting forth the pertinent provisions of the Act, this court, in reversing the judgment, said: "It is . . . very plain that the statute imposes the income tax on the proceeds of the sale of personal property to the extent only that *gains* are derived therefrom by the vendor, and we therefore agree with the Solicitor General that since no gain was realized on this investment by the plaintiff in error no tax should have been assessed against him. Section 2(c) is applicable only where a gain over the original capital investment has been realized after March 1, 1913, from a sale or other disposition of property."

This case was followed by *Walsh* v. *Brewster, supra.* In the first transaction there involved the taxpayer had purchased bonds in 1899 for $191,000, which he sold in 1916 for the same amount. Their market value on March 1, 1913, was $151,845. A tax was assessed on the difference between the latter amount and the selling price, namely, $39,155. This tax was held invalid, under the authority of *Goodrich* v. *Edwards,* on the specific ground that "the owner of the stock did not realize any gain on his original investment by the sale in 1916." In the second transaction involved the taxpayer had purchased certain bonds in 1902 and 1903 for $231,300, which he sold in 1916 for $276,150. Their market value on March 1, 1913, was $164,480. A tax was assessed upon the difference between the selling price and the market value of

the bonds on March 1, 1913. It was held, however, that "since the gain of the taxpayer was only the difference between his investment of $231,300 and the amount realized by the sale, $276,150," under the authority of *Goodrich* v. *Edwards*, "he was taxable only on $44,850," the difference between the purchase and sale prices.

These decisions are equally applicable to the Act of 1918. There is no difference in substance between the language of the two Acts in respect to the ascertainment of the gain derived or loss sustained from the sale of property acquired before March 1, 1913; and the correlative nature of these two provisions is emphasized in the Act of 1918 by their combination in one and the same sentence. As it was held in these decisions that the Act of 1916 imposed a tax to the extent only that gains were derived from the sale, and that the provision as to the market value of the property on March 1, 1913, was applicable only where a gain had been realized over the original capital investment, so we think it should be held that the Act of 1918 imposed a tax and allowed a deduction to the extent only that an actual gain was derived or an actual loss sustained from the investment, and that the provision in reference to the market value on March 1, 1913, was applicable only where there was such an actual gain or loss, that is, that this provision was merely a limitation upon the amount of the actual gain or loss that would otherwise have been taxable or deductible.

We cannot sustain the contention that the decision in *Goodrich* v. *Edwards* is not entitled to controlling weight in the matter of deductible losses because of the Government's confession of error, or because it involved the question of taxable gains, as to which it is said, that under a different construction of the Act a grave constitutional question would have arisen which could have no application to the question of deductible losses. The decision shows that it was not based on the confession of error or

on any constitutional question, but upon the conclusion that, as a matter of construction, it was "very plain" that the statute imposed a tax upon the proceeds of sales "to the extent only that gains are derived therefrom by the vendor." [6] The language of the opinion is specific and unambiguous; it embodied the reasoned judgment of the court as to the proper construction of the Act; and it applies equally to the construction of the similar provisions of the Act of 1918, relating to gains and losses alike.

This was recognized by the Treasury Department, which promptly amended its former Regulations by incorporating therein "the rule announced by the Supreme Court in the cases of *Goodrich* v. *Edwards* and *Walsh* v. *Brewster* respecting the basis for the determination of taxable gains or deductible losses in the case of property acquired prior to March 1, 1913, and sold or disposed of subsequent thereto." 23 T. D. 763, 764. To the same effect is the opinion thereafter given to the Secretary of the Treasury by the Attorney General in reference to taxable gains and deductible losses under both of the Acts. 33 Op. Atty. Gen. 291. And, it may be noted, a like construction has been independently given by the courts of New York, without reference to any constitu-

[6] It distinctly appeared from the Solicitor General's brief that the confession of error was not made because of any constitutional question, to which he made only an incidental reference, but because he was "forced to the conclusion" that, as a matter of construction of the Act, it was clear that it imposed a tax only on the "gains" derived from the sale of property, and that § 2(c) could have "no application until it is first ascertained, by comparing the purchase and selling prices, that there had been an actual gain." And this was followed by the statement that in the Government's view the similar provision relating to losses must be construed in the like manner, "that is, it must first be ascertained by comparing the purchase and selling price that a loss on the entire transaction has been sustained."

tional question, to the Income Tax Law of that State, in which the provisions relating to gains derived and losses sustained from the sale of property, are a substantial transcript of those of the Act of 1918, except that January 1, 1919, is substituted for March 1, 1913; this construction being embodied in a series of decisions, the first of which, relating to taxable gains, was written before those in *Goodrich* v. *Edwards* and *Walsh* v. *Brewster* were announced. *People ex rel. Klauber* v. *Wendell,* 196 App. Div. 827, affirmed, without opinion, 232 N. Y. 549; *People ex rel. Keim* v. *Wendell,* 200 App. Div. 388; *Re Application of Bush,* 206 App. Div. 800.

It is unnecessary to consider in detail, as in a matter of first impression, various contentions urged in behalf of the executors in respect to the construction that should be given to the provisions of the Act of 1918 in reference to deductible losses. For the reasons stated we think that the question should be resolved according to the earlier decisions; and nothing has been suggested which disposes us to depart from them now. Decisions affecting the business interests of the country should not be disturbed except for the most cogent reasons. *National Bank* v. *Whitney,* 103 U. S. 99, 102.

Since Flannery sustained no actual loss in the transaction in question, having sold the stock for more than it had cost, his executors were not entitled to the deduction which they claimed because it was sold at less than its market value on March 1, 1913.

The judgment of the Court of Claims is accordingly

Reversed.

MR. JUSTICE MCREYNOLDS and MR. JUSTICE SUTHERLAND dissent.